ANNUAL REPORT 1987

NOVA Corporation of Alberta

Incorporated in the province of Alberta, NOVA is a major Canadian shareholder-owned energy company headquartered in Calgary. NOVA's areas of business include gas transportation and marketing, petrochemicals, petroleum, manufacturing, consulting and research.

In 1987, the Corporation's assets of $4.7 billion generated $2.3 billion in sales and $179 million in net income. The NOVA companies employ about 7,100 people in Canada, the United States, Europe and Pacific Rim countries.

1987 Operations

- Petrochemical operations increased output significantly and cut production costs as commodity prices improved.
- The Alberta Gas Transmission Division moved a record 2.35 trillion cubic feet in 1987, and our gas marketing subsidiary had total sales of 293 billion cubic feet, up 34% from 1986.

1987 Financial

- Consolidated net income rose to $179 million from $100 million in 1986.
- Fully diluted net income per common share was 67 cents compared with 12 cents in 1986.
- Common equity increased to $1.3 billion as a result of the conversion of preferred shares and warrants to common shares, the issue of convertible debentures, and improved earnings.
- Favourable refinancing arrangements reduced costs to shareholders and pipeline tariffs considerably.

CONSOLIDATED FINANCIAL HIGHLIGHTS

(Thousands of dollars except for share data)

Year Ended December 31	1987	1986	% Change
Financial			
Revenue	$2,322,438	$2,680,966	(13)
Operating Income	$ 528,198	$ 573,221	(8)
Net Income	$ 179,130	$ 100,197	79
Net Income to Common Shareholders	$ 129,834	$ 16,126	*
Net Income Per Common Share			
Basic	$ 0.70	$ 0.12	*
Fully diluted	$ 0.67	$ 0.12	*
Common Shares Outstanding (Thousands)			
At Year End	211,484	141,841	49
Average	185,321	134,655	38
Common Equity**	$1,302,797	$ 648,707	*
Per Share	$ 5.76	$ 4.22	36
Return On Average Common Equity	13.3%	2.7%	*
Dividends Per Common Share	$ 0.40	$ 0.40	—

**Exceeds 100%* ***Includes convertible debentures and warrants*

The NOVA Logo

A-shaped for Alberta

Natural Gas Flame

Natural Gas Pipeline

Petrochemical Flask

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Annual Meeting

NOVA Corporation of Alberta's annual meeting will be held on Tuesday, April 26, 1988, at 10:30 a.m. in the Calgary Convention Centre, 120 Ninth Avenue S.E., Calgary, Alberta.

Rapports annuels en français

Veuillez vous adresser au secrétaire de la Compagnie si vous désirez recevoir un exemplaire de la version française de ce rapport.

It is a pleasure to report significant improvement in the Corporation's results for 1987.

Net income rose to $179 million or 67 cents a share, of which $54 million or 20 cents a share was earned in the fourth quarter.

The improvement resulted mainly from higher output and reduced costs throughout the Corporation's main business operations. The recent trend of price recovery for polyethylene, which is the commodity most important to NOVA's financial results, has been a positive factor. All of these favourable trends continue further, in early 1988.

Refinancing initiatives have lowered interest and preferred share dividend expense and have added to the Corporation's readiness to make the best of any foreseeable financial market and economy circumstance. A conservative financial strategy is being followed for the late 'eighties.

While there is genuine concern about worldwide economic conditions during the next few years, our earnings in 1988 are continuing to grow. NOVA gas transmission and petrochemical sectors are well based in Canada, and are very productive and efficient operations. We have a good opportunity to use our large investments in these two sectors to achieve record earnings in 1988, and in future years.

As a company relatively young with a large capital base, we believe that the management of assets is steadily improving.

The quarterly common share dividend, which was maintained at 10 cents per share during our lean earnings period of 1985 through mid-1987, is once again covered more than amply by current earnings and a dividend increase can be considered during 1988.

Pipelines, Petrochemicals and Petroleum

In the 1970s and early 1980s, we built NOVA's assets and revenues by making those investments which were perceived available and best at the time. During that period of aggressive growth, we moved into several new businesses which were seen as related to one another.

Some of those have proved to be highly desirable after several years of experience, while other investments and some project proposals have turned out to be relatively less relevant or timely than we intended and therefore have been disposed of, terminated or in some cases simply deferred for future performance when they may achieve better economic results.

The core business of NOVA itself has developed to be gas pipelines and petrochemicals. In those two businesses our people are experienced and proficient and have shown highly competitive abilities to work successfully in domestic and world markets. In each of those sectors, NOVA has shown that its organization is proficient at each stage including research and analysis, project conception, financing, project management and construction, operations, marketing and sales, and earning profits. Our application and development of new technology and production skills has become well recognized in the demanding and increasingly competitive world marketplace.

So NOVA goes forward in 1988, 1989 and 1990 as basically a pipeline and petrochemical company.

Some of our related and continued business lines such as valve manufacture have proven to be profitable even under the most difficult of industry conditions and will be maintained as supplementary activities. A small amount of our capital structure—but not more than one or two percent of our total assets—continues to be devoted to endeavouring to establish new and balancing business positions such as in NovAtel Communications Ltd.

The one other large investment position which NOVA maintains is its shareholding in Husky Oil Ltd. We see that and our smaller natural gas production investment in Novalta Resources Ltd. as maintaining a good position in the future evolution of Canadian-based oil and natural gas exploration and production, which should be very promising for the 1990s.

Husky is a medium-sized but very aggressive Canadian integrated oil company owned and equally controlled by NOVA and the Hong Kong-based group of companies led by Mr. Li Ka-shing. We believe that we will obtain really good future growth of asset values and financial performance through Husky.

Review of 1987

The earnings improvement in 1987 followed several years of depressed earnings linked mainly to low world petrochemical commodity prices and the start-ups of major investments. NOVA's common share price increased as the markets recognized both improved operating results and the inherent financial strength and stability of NOVA's businesses. Earnings for 1987 slightly exceeded management's 1987 budgeted expectations.

Additional small investments in ethylene and polyethylene facilities yielded significant improvements in production levels in 1987. These gains were augmented by strong operating performance which further exceeded expanded design capacity. Polyethylene operations also benefited from new marketing initiatives in Pacific Rim countries, significant engineering improvements and reduced feedstock costs. A sharp improvement in the price of methanol, which occurred in the second half of the year, allowed the Medicine Hat methanol complex to resume profitable full-scale production.

NOVA's gas transportation and marketing division continued to make steady and substantial contributions to earnings. A record 2.35 trillion cubic feet of natural gas was transported in and across Alberta in 1987, up over 10% from 2.13 trillion cubic feet in 1986. Early in 1988, a new record day receipt of 9.20 billion cubic feet was recorded. These volumes rank among the two or three largest throughput levels for pipeline systems in North America. The Corporation's marketing subsidiary, Pan-Alberta Gas Ltd., led the growth in export volumes among all Canadian marketers.

Late in 1987, NOVA elected to exercise its option to increase its ownership of Husky Oil Ltd. to 42.5% from 24.4% held after completion of the Husky reorganization earlier in the year. Husky was reorganized as a private company governed by a shareholder agreement, with ownership/control held equally by NOVA and a publicly traded Hong Kong company group. We believe this

◂ *From its head office in Calgary, Alberta, NOVA is active worldwide in pipeline transportation, petrochemical production and marketing, oil and gas exploration and development, and related manufacturing ventures.*

arrangement will enhance our ability to achieve corporate goals and objectives for oil and gas investment.

In September 1987, NOVA completed the corporate restructuring of share equity initiated in the second quarter to provide its shareholders with rights and a share structure reflective of the major corporation NOVA has become. As a result, Class "B" common shares have been redeemed at par value and Class "A" common shares have been designated as common shares with full voting rights. The restructuring also provided for an increase in the number of NOVA directors up to 20, changed the corporate name to NOVA Corporation of Alberta and continued the Corporation under the Alberta Business Corporations Act.

Outlook for 1988

There are good prospects being developed for major investment and earnings growth for the future, some of which may be ready to start in 1988. The first of these could be the "Ethylene III project" which plans a 50% expansion of our ethylene production capacity in Alberta plus investment by NOVA and other international companies in a group of ethylene-using derivative plants in Alberta. The proposed investment, totalling over $1.5 billion by all participants, is subject to satisfactory assurance of ethane supply presently under review by the Energy Resources Conservation Board relating to the Alberta Government's policy. There is also the prospect of another round of major expansion of our natural gas pipeline facilities to transport a new higher level of deliveries of Alberta natural gas to the United States.

Husky Oil Ltd., which had already built a good position in recent years for increased Canadian oil production in the 1990s, is actively investigating additional opportunities for new investment action.

Such new investment expansion prospects could each add materially to further improvement of NOVA's results. However, each NOVA commitment will weigh the effects on current financial results as well as the additions to long-term asset position. NOVA has already earned a bright business future so we will approach with care our further building of a well-balanced, highly competitive and cost-efficient independent Canadian company positioned selectively for international and domestic trade.

Before considering such new prospects, NOVA's consolidated budget for capital expenditures in 1988 is $360 million, which includes $250 million for Alberta gas transmission facilities and $70 million for continuing capital programs to increase production and efficiencies in petrochemical plants.

On January 28, 1988, the Corporation announced its intention to acquire 24.8% of the voting shares of Polysar Energy & Chemical Corporation. The acquisition of these shares reflects the Corporation's assessment of the value of the shares as an investment, based on the earnings of Polysar Limited, a wholly owned subsidiary of Polysar Energy & Chemical Corporation involved in petrochemical production and marketing. On February 22, 1988, the Corporation acquired 13,004,175 shares of Polysar to hold 19,004,175 shares representing approximately 31% of the common shares or 24.8% of the total voting securities of Polysar.

Management Direction

NOVA management highlights the following 1988 objectives:

- To concentrate our investment opportunities in three sectors: pipelines, petrochemicals and through our affiliated company, Husky Oil Ltd., in petroleum.
- To achieve earnings per share in excess of $1 per common share which would result in a return on common equity in excess of 17%, up from 13% for 1987.
- To continue rigorous control of expenses and overhead costs.
- To finance expansion conservatively and maintain or improve the current long-term debt to common equity ratio of 1.9 to 1.
- To improve operations and products with cost-effective applied research and development at a level of at least 5% of after-tax profit.
- To maintain an early lead in pipeline engineering, petrochemical commodities and telecommunications in China and other Asian markets.
- To maintain a high standard of environmental, safety and fair and productive employment practice in all NOVA companies.

A substantial gain in NOVA's 1987 overall performance was due largely to major successes in both operating and marketing initiatives by the Corporation's petrochemical business.

Board and Management

Mr. Ronald B. Coleman, consultant, joined the Board in June 1987. In February 1988, the Board received with regret and appreciation of their services the resignations of Messrs. Edward W. Best and John R. McCaig as directors.

The two executive vice presidents of NOVA, Messrs. James H. Butler and William G. Wilson, were appointed to the Board in January 1988. Jim Butler and Bill Wilson have each made important contributions to NOVA's progress in the past year and have broadly increasing responsibilities in its management.

Our hard-earned franchise through Foothills Pipe Lines (Yukon) Ltd. for the current substantial movement of Alberta natural gas to the United States through its prebuild sections and for the future movement of natural gas supply from the northern gas production areas of North America will be even more highly valuable in the next years and has been maintained. These major projects were the responsibility of our president, Bob Pierce, who also chaired the energy sectoral committee advising the Government of Canada for the free trade negotiations with the United States.

The other officers, managers, professionals, technical, operations and office staffs in NOVA have done well again in 1987. They are commended for their many individual specific contributions to the improvements that we have the honour to record in this annual report.

Respectfully submitted on behalf
of the Board of Directors,

S. R. Blair
Chairman and Chief Executive Officer

February 23, 1988

H.J.S. Pearson *P.L.P. Macdonnell, C.M.*
A.J.E. Child, O.C. *H.N. Hotchkiss*

S.R. Blair, C.C. *W.A. Howard* *R.H. Carlyle* *J.J. Healy* *R.L. Pierce* *J.R. McCaig* *W.H. Comrie*

F.A. McKinnon *R.B. Coleman* *D.K. Seaman* *E.W. Best*

Edward W. Best
Partner, Foster Research, Calgary, Alberta
(Economic Research)

S. Robert Blair, C.C.
Chairman and Chief Executive Officer
of the Corporation

R. Harold Carlyle
Retired, Calgary, Alberta

Arthur J.E. Child, O.C.
Chairman and Chief Executive Officer,
Burns Foods Limited, Calgary, Alberta
(Food Processor)

Ronald B. Coleman
President, R.B. Coleman Consulting Ltd.,
Calgary, Alberta
(Oil and Gas Consulting)

William H. Comrie
Chairman,
The Brick Warehouse Ltd.,
Edmonton, Alberta
(Home Furnishings Distribution)

J. Joseph Healy
President, Healy Motors Limited,
Edmonton, Alberta (Transportation)

Harley N. Hotchkiss
President, Harman Resources Ltd.,
Calgary, Alberta (Private Investor–
Oil and Gas, Real Estate and Agriculture)

William A. Howard
Senior Partner, Howard, Mackie,
Calgary, Alberta
(Barristers and Solicitors)

Peter L.P. Macdonnell, C.M.
Partner, Milner & Steer,
Edmonton, Alberta
(Barristers and Solicitors)

John R. McCaig
Chairman and Chief Executive Officer,
Trimac Limited, Calgary, Alberta
(Transportation and Resource Services)

Fred A. McKinnon
Retired, Calgary, Alberta

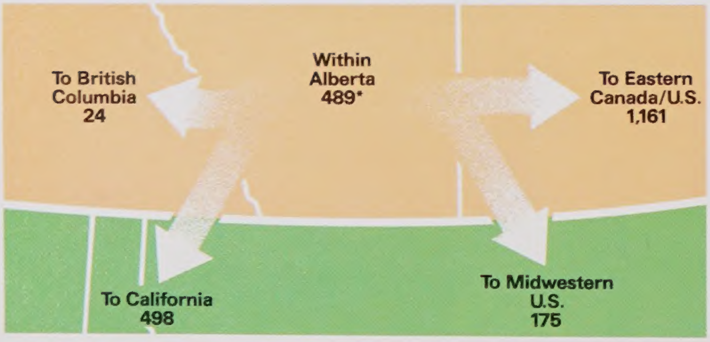
H.J. Sanders Pearson
Vice Chairman of the Corporation;
Chairman, Century Sales & Service Limited,
Edmonton, Alberta
(Industrial Tools and Fasteners Distribution)

Robert L. Pierce
President of the Corporation

Daryl K. Seaman
Chairman and Chief Executive Officer,
Bow Valley Industries Ltd.,
Calgary, Alberta (Natural Resource
Services, Exploration and Development)

GAS TRANSPORTATION IN ALBERTA

NOVA SYSTEM GAS DELIVERIES
(Billion cubic feet–2,347 total)



*Includes pipeline usage

Gas Transportation & Marketing

Total marketed Canadian gas production increased about 7% to an estimated 2.7 trillion cubic feet, largely because of increased demand from the United States.

Deregulation of natural gas pricing resulted in innovative marketing initiatives and extensive negotiations with end users which contributed to increased export sales of Canadian gas in 1987.

Average prices received by gas producers declined because of surplus supplies and intense competition for natural gas contracts in all markets.

Review of 1987

NOVA's investments in natural gas transportation and marketing include the gas transmission system in Alberta and Novacorp Pipelines Ltd., both 100% owned, and 50% ownership of Foothills Pipe Lines (Yukon) Ltd., Pan-Alberta Gas Ltd. and Trans Québec & Maritimes Pipeline Inc. In 1987, this sector comprised about half of the Corporation's consolidated assets and revenue and over 60% of operating income.

NOVA's Alberta pipeline system carries more than 10% of the gas produced annually in North America and over 75% of all marketed Canadian gas.

Total volumes transported through NOVA's Alberta system during the past calendar year were up over 10%, setting a new record of 2.35 trillion cubic feet. NOVA shipped 2.13 trillion cubic feet of gas in 1986 and 2.25 trillion cubic feet in 1985, the previous record year. Leading the increase were deliveries to the Alberta industrial market and to customers in California and the midwestern states.

Some 1.86 trillion cubic feet were exported from Alberta in 1987, including 497.8 billion cubic feet to California and 175.1 billion cubic feet to the U.S. midwest via the Foothills pipeline system. Deliveries in Alberta totalled 483.5 billion cubic feet, up 5% from 1986.

As a result of higher volumes, reduced financing charges and ongoing cost control, NOVA's transportation service rates for exports from the province averaged 25 cents per thousand cubic feet in 1987, down from 27 cents in 1986.

In August, NOVA reduced its rate of return on its $1.3 billion rate base for Alberta gas transportation operations to 11.49% from 12.91% because of initiatives taken to reduce financing costs. The new rate, set after discussions initiated by NOVA with its customers and other interested groups, incorporates a 13.25% after-tax return on a deemed 32% common equity component. NOVA has reduced its charges to the producing industry four times in as many years.

Pipeline investment in 1987 included expansion and improvements to the existing system, with capital spending of over $70 million. Approximately 123 miles of pipeline and related metering facilities were installed.

At December 31, 1987, NOVA's Alberta system comprised 8,805 miles of pipeline, 36 compressor stations and 825 major receipt and delivery points.

Novacorp Pipelines Ltd., 100% owned, builds, owns and operates pipelines on a contract basis to meet customer requests for service outside the parameters of NOVA's gas transmission system. In 1987, the company completed a 100-mile gas liquids pipeline in the Porcupine Hills area of southern Alberta. Novacorp Pipelines has total pipeline assets of about $30 million.

Phase I of the Alaska Highway Gas Pipeline system, owned and operated by Foothills, delivers Alberta gas to markets in the United States. The pipeline was built as the first phase of a major system to bring Alaska gas to market in the lower 48 states. The system's western leg operated at full capacity of 240 million cubic feet a day in 1987 and the eastern leg, with contracted capacity of 975 million cubic feet a day, operated at about 48% of contracted capacity. Throughput on the eastern leg increased in 1987 by 95%, primarily because of Pan-Alberta Gas marketing initiatives.

At December 31, 1987, the eastern and western legs comprised 528 miles of pipeline, four compressor stations and two meter stations. The rate of return was 10.9% on an average rate base of $631 million, with an after-tax return, excluding an incentive return, of 14.25% on a 25% equity component.

Pan-Alberta Gas, the largest independent Canadian marketer of gas to the United States, had total sales of 293 billion cubic feet in 1987, up 34% from 219 billion cubic feet in 1986. For the third year in a row, Pan-Alberta's customer in California purchased all of the gas allowed under its contract. About 88% of Pan-Alberta's gas sales are to the U.S. market.

Pan-Alberta has about 1,200 contracts with some 420 Alberta producers. During 1987, the company continued its adjustment to the deregulated environment by aggressively seeking new short- and long-term markets for Alberta gas.

Trans Québec & Maritimes Pipeline, which transports gas in the province of Quebec, carried about 93 billion cubic feet in 1987, up slightly from 90 billion cubic feet in 1986. At December 31, 1987, TQM facilities comprised 213 miles of pipeline, 10 meter stations and five sales taps. The rate of return is 13.11% on a rate base of $383 million, with a 13.75% after-tax return on a 25% equity component.

Outlook for 1988

Increased demand for Alberta gas in both Canada and the United States is expected to spur increased gas transmission and marketing volumes for NOVA in 1988, with gas volumes projected to increase over 1987 record levels.

Capital spending on the pipeline system, driven by customer requests for increased capacity, is budgeted at about $250 million in 1988. Deregulation has resulted in continued growth in numbers of customers and contracts for the Alberta system and this trend is expected to continue in 1988.

Pan-Alberta expects to increase its sales in 1988 through continued aggressive marketing strategies. To accommodate anticipated volume increases, Foothills is expected to apply to the National Energy Board for permits to expand its eastern leg beyond current capacity of 1.1 billion cubic feet a day. The eastern leg was originally designed to carry 1.8 billion cubic feet a day, and can be expanded to the design capacity at relatively low cost.

Foothills remains committed to the completion of the Alaska Highway Gas Pipeline in the mid-1990s. Ongoing cost studies indicate the pipeline system will cost substantially less than originally envisaged.

NOVA moved record volumes of Alberta natural gas in 1987 as a result of increased demand for exports to the United States

Petrochemicals

The petrochemical industry experienced a recovery in 1987 after several years of depressed prices linked to oversupply conditions around the world.

Increased demand for polyethylene, ethylene and methanol, NOVA's primary products, resulted in higher sales volumes and prices for these commodities. Polyethylene prices throughout the year were about 23% higher than in 1986. Growth in demand for polyethylene led both ethylene and polyethylene manufacturers to operate at capacity. Methanol prices also increased sharply, exceeding the 1986/87 average by 50% as demand came into balance with supply.

The improved demand results from new markets in developing countries and growth in the use of plastics in industrialized countries.

Review of 1987

NOVA's petrochemical investments include facilities for the production of ethylene, polyethylene and methanol from natural gas, as well as ethane extraction and gathering systems, product pipelines and storage facilities. In 1987, this sector accounted for about a quarter of the Corporation's consolidated assets, 44% of revenue and nearly 40% of operating income. These investments are managed by wholly owned Novacor Chemicals Ltd.

NOVA is the largest producer and marketer of ethylene and polyethylene in Canada, with about 58% of current Canadian ethylene capacity and 41% of polyethylene capacity. Ethylene, the major building block for the petrochemical industry, is made from ethane, which is extracted from natural gas. NOVA upgrades ethylene to produce a full range of polyethylene products. Petrochemical products are marketed in Canada, the United States, China and Pacific Rim countries.

Operating results for the petrochemical division improved substantially in 1987 due to gains in productivity, lower manufacturing costs and a strong upturn in world petrochemical markets.

◂ *Production of ethylene and polyethylene exceeded design capacity at NOVA's facilities near Joffre, Alberta, as the industry experienced strong recovery.*

NOVA's petrochemical investments showed significant improvement in operating results in 1987 and industry conditions are projected to continue strong in 1988

Price increases for polyethylene—our major product—plus significant technological improvements and lower ethylene costs, allowed Novacor to increase production and cut costs during a period when worldwide product demand achieved balance with industry capacity.

NOVA's annual petrochemical plant capacity now stands at 3 billion pounds of ethylene, 800 million pounds of linear low-density polyethylene, 230 million pounds of high-density polyethylene and 200 million pounds of conventional low-density polyethylene. Two ethylene plants and a linear low-density polyethylene plant are located at Joffre, Alberta. NOVA also owns a polyethylene plant near Sarnia, Ontario.

The ethylene business, conducted under long-term, take-or-pay supply contracts with prices based on cost-related demand/commodity charges, continued to contribute steadily to profit. Production at the Joffre plants exceeded design capacity by an average of 5% in 1987. Higher operating rates allowed NOVA to provide lower cost ethylene to long-term customers.

Since the state-of-the-art ethylene and polyethylene plants were opened, significant cost savings and increases in throughput have been achieved. Ethylene capacity has been increased by 300 million pounds over the original design capacity without major capital investment. Polyethylene production capacity from the original Joffre plant has been increased by 200 million pounds, also at minimum cost, and during 1987, the plant operated at 5% above the new design capacity.

Additional programs are under way to further increase output from the ethylene plants and the Joffre polyethylene plant. At the Sarnia plant, changes to the product mix have yielded more efficient operations and plans are being implemented to increase output of specific polyethylene products.

Also during 1987, Novacor completed and began operating new facilities at Joffre, including a hydrogen plant and an addition for pelletizing polyethylene.

Hydrogen, formerly used as fuel in the ethylene plants, is recovered and sold for use in a nearby ammonia plant. Contracts provide assured return on investment plus coverage of both capital and operating costs. The pelletizing facility allows linear low-density polyethylene, previously available only in granular form, to be produced as a uniform product that can be shipped more cost effectively. Both projects were completed on time and under budget.

The petrochemical industry turnaround also improved operating conditions for NOVA's investments in production and marketing of methanol. NOVA owns 50% of Alberta Gas Chemicals Ltd., which operates three methanol plants at Medicine Hat, Alberta, with a combined design capacity of 2,400 short tons per day.

The most efficient plant, with design capacity of 1,200 short tons per day, continued operations throughout the year. On the strength of price increases late in the year, the other two plants were reopened and all three plants are operating at full production rates.

Outlook for 1988

NOVA's petrochemical interests will reflect a significant improvement in operating results as industry conditions continue to improve in 1988.

Polyethylene prices, which bottomed in mid-1986 then strengthened in 1987, are expected to remain strong and continued growth in demand is forecast. While demand strengthens, no significant new polyethylene capacity will be added to world production levels in 1988 and little new capacity will come on stream over the next four years.

Plans are under way to build a third ethylene plant once feedstock supplies can be assured and sales contracts signed for the plant's planned annual output of 1.5 billion pounds. The third plant could begin operating in 1991. Construction of new ethylene facilities would be based on the dedication of plant output under long-term supply arrangements. Meanwhile, ethylene and polyethylene capacity will be increased through debottlenecking and incremental expansion of existing facilities.

NOVA's investments in methanol production and marketing are also expected to show increased profitability in 1988 because of significant price increases, resulting from increased demand combined with reduced production capacity around the world.

Petroleum

The significant decline in world oil prices during 1986 has challenged the petroleum industry to adapt to a new economic environment for energy.

Although crude prices, fiscal conditions and operating efficiencies have improved in 1987, the current pricing environment remains unstable. As a result, the industry must continue to be highly selective in the allocation of capital resources.

Review of 1987

NOVA's petroleum activities are conducted by Husky Oil Ltd., 42.5% owned, and Novalta Resources Ltd., 100% owned.

Husky is an integrated Canadian oil and gas company engaged in exploration, development, production, refining, marketing and transportation of crude oil and natural gas. In addition, Husky continues to position for the future and now has quality exposure in the key Canadian industry segments of heavy oil, in situ oil sands, the Beaufort Sea, East Coast offshore and Alberta's Foothills deep gas area.

In 1987, Husky's light and medium oil and natural gas exploration efforts in the western Canada basin were centred on targets which provide good prospective returns under current prices as well as strong upside economic potential. Husky participated in 23 exploration wells, resulting in 13 oil wells and one gas well.

A particular success during 1987 was Husky's involvement in a significant gas discovery on Husky farm-out lands near Caroline, Alberta. The discovery well tested high sustained rates of natural gas. When fully developed, this field may be the largest of its kind in western Canada. Two step-out wells to the original gas discovery were drilled and tested excellent results, further confirming the potential of this major discovery. Husky is actively pursuing follow-up targets that are based on high technology seismic evaluation.

NOVA continues to seek quality prospects in oil and gas exploration and production in Canada through its successful petroleum investments in Husky Oil Ltd. and Novalta Resources Ltd.

As part of Husky's evaluation of quality medium- and long-term prospects, heavy oil exploration in 1987 centred on the Caribou Lake block about 120 miles north of Lloydminster, Alberta. This 238,000 acre block contains large deposits of bitumen and the property further integrates and supplements Husky's extensive Lloydminster operations. Since the inception of the Caribou Lake exploration program, about 300 miles of seismic have been shot and 31 wells have been drilled. Results to date are encouraging and support Husky's view that the lands have excellent future production potential.

Husky believes that major oil and gas reserves, capable of contributing significantly to North American energy supply, will most likely be developed from frontier discoveries and international areas. Primary frontier activities in 1987 included further delineation drilling on the Amauligak structure in the Beaufort Sea and delineation drilling on the Whiterose structure on the East Coast offshore.

In the Beaufort Sea, a berm has been built to facilitate drilling and the first well to be drilled from this location, F-24, was spudded on October 1, 1987. With a 17.5% working interest, Husky is the second largest participant in the field. The prospect is currently estimated to contain the largest recoverable oil potential in the Beaufort Sea with estimates ranging from 400-800 million barrels of recoverable oil.

On the Grand Banks off Canada's East Coast, a third Whiterose delineation well, Whiterose E-09, is being drilled. In 1987, additional East Coast exploration activities included the drilling and testing of the North Ben Nevis M-61 delineation well on the Grand Banks, and the drilling of the Bonne Bay C-73, also on the Grand Banks, which was abandoned.

In 1987, total gross production of crude oil and natural gas liquids averaged 41,700 barrels per day; light and medium crude oil and natural gas liquids averaged 13,600 barrels per day; and heavy oil production averaged 28,100 barrels per day. Natural gas sales averaged 61.2 million cubic feet per day.

Husky is involved in all aspects of downstream petroleum operations, continuing a program of modest long-term growth. Refined product sales in 1987 averaged 13,200 barrels per day of light oil and 8,200 barrels per day of asphalt and residuals, which are comparable to 1986 sales. Blended crude oil sales of 96,200 barrels per day provided steady contributions to downstream profit.

Through its petroleum investments NOVA continues to develop a balanced, quality exposure to key petroleum opportunities

Novalta Resources is engaged in oil and gas acquisition, exploration, development and production, and gas marketing, with activities centred in Alberta. Novalta increased its gas sales by 25% in 1987, and reached a new record peak day sales rate of 70 million cubic feet per day in December. Novalta also manages deliveries to various industrial markets in Alberta and moved a record 110 million cubic feet per day in December. Market growth included the initiation of deliveries to a hydrogen off-gas project at Joffre, Alberta.

Consistently successful since its formation in the mid-1970s, Novalta continued to show an operating profit in 1987 despite generally poor industry conditions.

Gas production averaged 41 million cubic feet per day, compared with 32 million cubic feet per day in 1986. Oil and natural gas liquids production averaged 942 barrels per day, compared with 692 barrels per day in 1986. Landholdings total 1.1 million gross (550,000 net) acres.

Outlook for 1988

Through its petroleum interests, NOVA continues to pursue quality investments which include conventional oil and gas exploration and development, and further evaluation of quality long-term petroleum prospects.

Husky has successfully adjusted to the fundamental changes in the operating environment and will continue to pursue and capitalize on short- and medium-term investments while furthering efforts to position itself for long-term opportunities.

Novalta Resources will continue to direct its expansion efforts to the enhancement of its natural gas supply capability to serve selected markets, most particularly as a supplier to the Alberta industrial sector, including NOVA's petrochemical businesses. Under the careful direction of management, capital spending will increase modestly in 1988 as Novalta positions itself for anticipated improvement in the profitability of the natural gas producing sector.

Other Businesses

In addition to its primary businesses, NOVA has interests in international consulting, energy-related manufacturing, telecommunications, and research and development.

International consulting and manufacturing activities remained stable, although new opportunities related to pipeline construction continued to be restrained by reduced energy development.

Markets for pipeline consulting and products in North America are generally related to increasing system efficiency and safety. This situation is also prevalent internationally, although there are a few pipeline projects directed toward increased use of indigenous resources, industrial development and environmental considerations.

The telecommunications business continued to expand in 1987 as demand for cellular systems and telephones strengthened in major markets.

Review of 1987

Novacorp International Consulting Ltd., 100% owned, provides engineering, technical and operating consulting services in pipeline transportation and markets specialized pipeline products. Novacorp's expertise and products are based on experience related to project management, construction and operation of NOVA's gas transportation system, which is recognized as one of the most technologically sophisticated in the world.

In 1987, Novacorp continued to provide project management and engineering expertise in Malaysia and Turkey on two of the world's major pipeline projects currently in progress. Novacorp is also involved in pipeline development in several other countries, including China, Australia, Finland and Colombia. Novacorp has focused its marketing activity on selected key areas and increased its emphasis on specialty products such as mechanical dry seals and magnetic

◀ *NOVA continues to improve its operations and products with cost-effective applied research and development activities conducted by Calgary-based NOVA HUSKY Research Corporation Ltd. and through commitments to other research organizations.*

NOVA's other businesses will contribute increased profits in 1988 as a result of cost-conscious management and closely targeted marketing programs

bearings based on its extensive knowledge of the international pipeline industry.

Novacorp was awarded 41 contracts in 16 countries in 1987 and is bidding and negotiating on other projects around the world.

Grove Italia S.p.A., 100% owned, manufactures pipeline valves and flow control products in the United States and Italy for worldwide sale to the energy industry. The valve group maintained its consistent profitability last year in an industry where virtually every other major participant operated at a loss. Financial results were positive despite a slight decline in revenue and continued pressure on margins from international sales. The company eliminated debt and continued cost-conscious management practices to reflect current market realities and position itself for improved performance.

NovAtel Communications Ltd., 50% owned, is the only manufacturer of cellular systems and telephones in Canada. Formed in 1983, it has grown rapidly despite strong competition from established international telecommunication companies. NovAtel, headquartered in Calgary, also has offices in Toronto, Montreal and the United Kingdom.

Revenue increased by over 60% in 1987, with NovAtel strengthening its position as one of the largest suppliers of cellular telephones to the United States market, where sales accounted for 55% of revenue. NovAtel also installed and contracted for 16 cellular telephone systems in the United States during 1987. Other systems were installed in western Canada, the Northwest Territories and Chongqing, China. The company also markets its products in the United Kingdom, Australia, New Zealand, Bermuda and Costa Rica.

NovAtel's strong emphasis on quality control produces highly reliable and durable products. In addition, the company continues to support ongoing research and development programs that supplement its position on the leading edge of telecommunications technology. In September 1987, NovAtel was awarded a gold medal in the annual Canada Awards for Business Excellence, winning top honours in the category of industrial design for its 8300/9300 series of cellular telephones.

NOVA's business objectives are supported by the work of NOVA HUSKY Research Corporation Ltd., which continues to pursue research and development activities for its owners and their affiliates. Research focuses on pipeline, petrochemical and petroleum technology. Areas under study in 1987 included natural gas dynamics, enhanced recovery and upgrading of heavy oil, and improved production of a wider range of petrochemical products.

NHRC is currently conducting nearly 100 research projects. Five patent applications for new technology were filed in 1987. New products include a dew point monitor to measure automatically the temperature at which dew forms in a pipeline and a remote terminal unit that facilitates data collection. Research by NHRC was instrumental in increasing polyethylene production at NOVA's petrochemical facilities.

Outlook for 1988

Novacorp, established as a reputable and reliable engineering consulting company, will focus its marketing efforts on specialized products and consulting services in North America and on large pipeline developments in targeted international areas.

Grove Italia expects the U.S. market for valves and flow control products to improve in 1988. The international market will continue to fluctuate according to the rate of energy industry activity. Grove will remain profitable and continue to position itself for increased growth as the industry recovers.

NovAtel expects to increase sales of both terminals and cellular systems as a result of aggressive marketing programs around the world. Quality and cost control and development of new technology will continue to be a high priority.

NHRC will continue to participate in new product development and efforts to enhance the productivity of assets in petrochemical, gas transmission and petroleum operations.

NOVA is committed to providing a safe, productive business environment for its employees, customers and the general public.

To accomplish this corporate objective, NOVA has established policies and programs dedicated to community and employee relations in such areas as corporate contributions, occupational health and safety, environmental affairs, and employee motivation and development.

We believe shareholders have a special interest in corporate policies and practices. Because some of these assumed a particularly important role in 1987, we have chosen to comment on them in this report.

Corporate Contributions

As a major part of our ongoing program of corporate support for non-profit community-based organizations where NOVA has business operations, NOVA participated as a corporate sponsor of the XV Olympic Winter Games, held in Calgary in February 1988.

NOVA agreed to sponsor the games because the Corporation is one of the few major Canadian companies headquartered in Calgary. We believe it fitting that an international event of this high calibre be supported by a company that prides itself on its Alberta base and international scope of operations.

Our sponsorship obligations were met through support that NOVA was uniquely positioned to provide. Allotment of space in NOVA facilities, provision of goods and services, and secondment of several key technical staff members to groups responsible for organizing and managing the games were the main components of NOVA's sponsorship. Another major contribution was the underwriting of novaplayRites'88, part of the Olympic Arts Festival, which provided a Calgary-based theatre group with the opportunity to produce five new Canadian plays. On their own time, NOVA employees also provided support as volunteers, some playing major roles in the organization and staging of the games.

◀ *NOVA employees supported the XV Olympic Winter Games, held in Calgary during February 1988, by providing their time and expertise on a volunteer basis to the groups responsible for organizing and staging the games.*

NOVA's corporate contributions program is planned, organized and implemented by a committee of NOVA employees which allocates donations in five major areas: health and welfare, education, arts and culture, community relations and recreation.

In 1987, particular emphasis was placed on health and welfare donations to local and provincial organizations which experienced a high demand for services at a difficult time in Alberta's economy. As a second priority, NOVA also provided long-term support to Alberta and other educational institutions for faculties of management, engineering, native education and medicine. This support is intended to help develop important human resource skills for Alberta and Canada.

Funding of projects in smaller communities where NOVA has a presence considers the input of local management and employees who are closely involved in these communities. In addition, NOVA continues to support the substantial involvement of its employees in charitable causes that benefit the communities in which they reside.

NOVA's long-term success is supported by its willingness and ability to benefit and enrich communities in which operations are located

Occupational Health, Safety and Environmental Affairs

NOVA's operations are characterized by an ongoing commitment to occupational health and safety and to preservation of the environment.

The NOVA group of companies has a very low accident rate relative to other companies and industries in Canada. The Corporation maintains occupational health and safety and environmental affairs departments staffed with professionals and our experience and professionalism has earned NOVA a positive reputation for environmental management. All levels of NOVA management promote and encourage safe work practices and environmental responsibility as productive management practices.

Trained personnel play a key role in all aspects of construction and operation of facilities to ensure that new plants and operations meet high health, safety and environmental standards for employees and the general public. Occupational health and safety activities include periodic health assessments, ongoing review of working environments, treatment, diagnosis, health education and counselling through a wide range of programs. Environmental activities include conducting impact studies, obtaining construction permits, ensuring that reclamation programs are implemented when projects are completed, and monitoring operations. Research and development studies on issues such as soil conservation and chemical usage are an integral part of environmental planning.

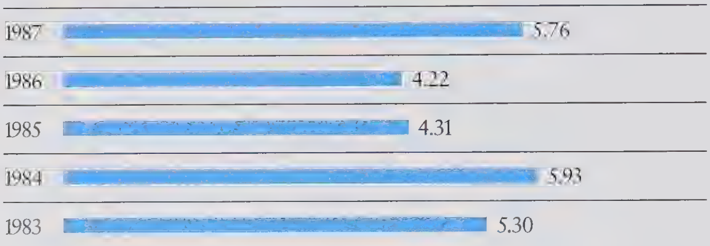
Human Resources

The Corporation's central human resource objective is to create and maintain an environment in which employees optimize talents and skills in the most productive manner possible, to the mutual benefit of the employee and the Corporation.

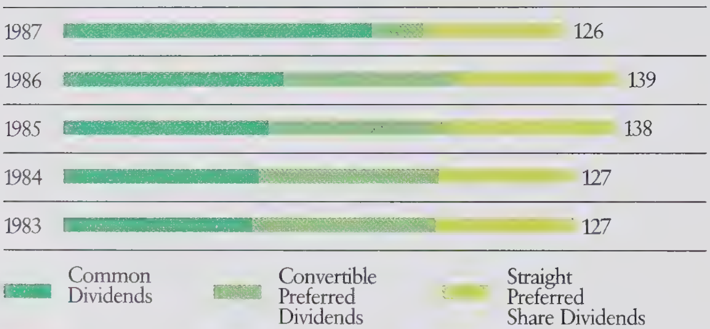
NOVA has long-standing policies in support of non-discriminatory hiring, compensation and employee development which reinforce performance as the key to career development. By integrating operating plans of NOVA companies with employee performance and development assessment, employees are exposed to diverse career opportunities. The depth of talent in NOVA companies and the emphasis on performance-based human resource management support a high level of productivity and career development.

We are proud of the very positive employee relations which NOVA enjoys and of the pride that NOVA employees take in representing the Corporation. Considerable achievements in reducing costs and improving productivity in 1987 are a reflection of the capability, motivation and commitment of NOVA's employees. In addition to these accomplishments in 1987, NOVA employees have again achieved recognition professionally and internationally as individuals and in bringing awards to NOVA companies.

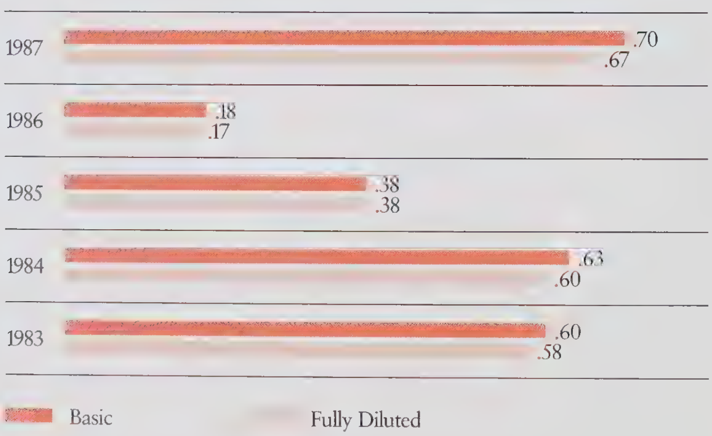
For 1988 the Corporation will continue efforts to develop employees through management and skill training geared to the attainment of corporate goals.



COMMON EQUITY PER SHARE AT YEAR END
(Dollars)



DIVIDENDS FOR THE YEAR
(Millions of dollars)



NET INCOME PER COMMON SHARE FOR THE YEAR*
(Dollars)

**Before extraordinary items*

SHAREHOLDER INFORMATION

NOVA welcomes questions from shareholders and potential investors, which may be directed to senior officers or to the corporate finance department by writing or telephoning the Corporation's head office. NOVA's toll-free number (800) 661-8686 may be used by Canadian callers outside of Calgary.

Literature on various aspects of the Corporation's business is also available and may be obtained by writing to our head office address or by calling our toll-free number.

Share Issues

NOVA shares are listed on the Toronto, Montreal and Alberta stock exchanges. The Corporation's common shares, which are widely held by private sector investors, are among the most actively traded securities in Canada. In 1987, more than 132.3 million shares were traded, representing a total dollar value of about $1.2 billion.

At December 31, 1987, a total of 211.5 million common shares were outstanding. In addition, eight preferred share issues were outstanding.

Share Registration

Common shares are registered with the Vancouver, Edmonton, Calgary, Regina, Winnipeg, Toronto and Montreal offices of National Trust Company. Preferred shares are registered as follows: Canada Trust Company in Vancouver, Calgary, Edmonton, Regina, Winnipeg, Toronto and Montreal for all share issues; and Canada Trust Company in Halifax (7.60%, 6-3/8%, 11.24%, 9-1/8% preferred shares only). The 1996 warrants are registered with the Vancouver, Edmonton, Calgary, Regina, Winnipeg, Toronto, Montreal and Halifax offices of Montreal Trust Company.

Holders of NOVA securities may receive more than one copy of our annual and quarterly reports. Duplication cannot always be avoided because our common shares and preferred shares are registered with two transfer agents. Holders of common shares who receive more than one document due to differences in registered names or addresses should contact National Trust to have their holdings consolidated. Those holders of any issue of preferred shares in the same

situation should make similar arrangements with Canada Trust.

Share Designations

NOVA's share issues are designated in newspaper listings as follows:

Nova Cor f		Common
Nova C	p	4-3/4% Series C Preferred
Nova E	p	7-3/4% Preferred
Nova F	p	9-3/4% Preferred
Nova G	p	9.76% Preferred
Nova H	p	7.60% Preferred
Nova J	p	6-3/8% Second Preferred
Nova N	p	11.24% Preferred
Nova O	p	9-1/8% Preferred
Nova W		1996 Warrants

Dividend Reinvestment Plan

NOVA's dividend reinvestment and share purchase plan provides a convenient method for shareholders to reinvest dividends automatically on all or some of their NOVA common and preferred shares at the weighted average of the selling price of common shares on The Toronto Stock Exchange for the five trading days prior to the dividend payment date. It also allows shareholders to make cash payments of $50 to $5,000 per quarter to buy common shares at the same average price.

Both options are offered to shareholders without brokerage or administrative fees attached. The plan is not available to residents of the United States. Additional information may be obtained from the transfer agent charged with plan administration: National Trust Company, Corporate Trust Services, Suite 1008, 324 Eighth Avenue S.W., Calgary, Alberta, T2P 3B2. Information may also be obtained from NOVA's corporate finance department.

The Corporation's annual meeting will be held on Tuesday, April 26, 1988, at 10:30 a.m in the Calgary Convention Centre, 120 Ninth Avenue, S.E., Calgary, Alberta

NOVA Group Officers

Corporate Officers

S. Robert Blair
Chairman and Chief Executive Officer

H. J. Sanders Pearson
Vice Chairman of the Board

Robert L. Pierce
President

William G. Wilson
Executive Vice President and Chief Financial Officer

James H. Butler
Executive Vice President

Bruce W. Simpson
Senior Vice President

Richard C. Milner
Vice President, Treasurer and Corporate Secretary

John W. F. Cowell
Vice President

Alex W. Kabatoff
Vice President

Brian F. Olson
Vice President

Joan A. Dennis
Assistant Secretary and Secretary to the Board

Thomas G. Milne
Assistant Treasurer

Alberta Gas Transmission Division

Donald G. Olafson
Division Senior Vice President

Robert B. Snyder
Division Senior Vice President

Principal Subsidiaries and Affiliates

James H. Butler
Chairman and Chief Executive Officer, Novacor Chemicals Ltd.

Gordon W. Cameron
President and Chief Executive Officer, Pan-Alberta Gas Ltd.

John E. Feick
President, Novacor Chemicals Ltd.

Luigi Fiore
Chairman, Grove Italia S.p.A.

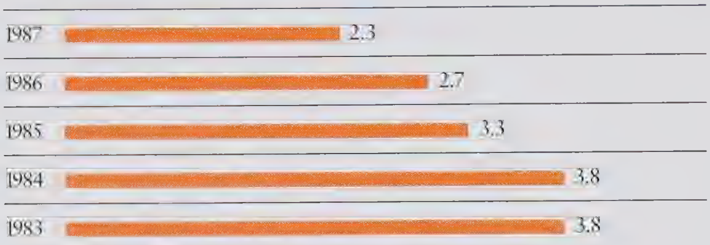
C. Kent Jespersen
President, Foothills Pipe Lines (Yukon) Ltd.

Del Lippert
President and Chief Executive Officer, NovAtel Communications Ltd.

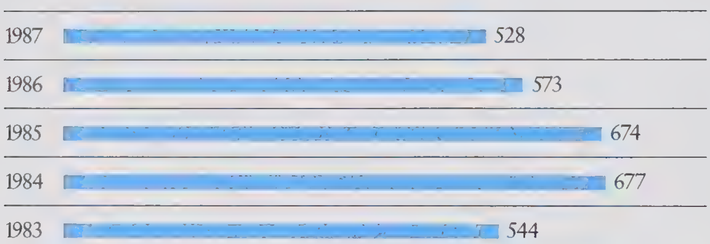
Donald G. Olafson
President, Novacorp International Consulting Inc.

Arthur R. Price
President and Chief Executive Officer, Husky Oil Ltd.

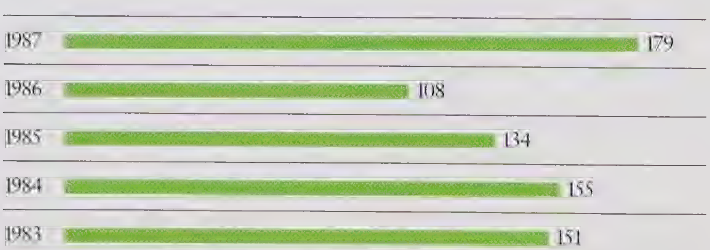
CONSOLIDATED REVENUE FOR THE YEAR
(Billions of dollars)



CONSOLIDATED OPERATING INCOME FOR THE YEAR
(Millions of dollars)



CONSOLIDATED NET INCOME FOR THE YEAR*
(Millions of dollars)



**Before extraordinary items*

NOVA's strong financial performance in 1987 was highlighted by a major increase in common equity and the achievement of a new record in net income to common shareholders.

Consolidated Net Income

Consolidated net income was $179.1 million, up from $100.2 million in 1986. Fully diluted net income per common share was 67 cents compared with 12 cents per common share in 1986. Basic net income per common share was 70 cents on a total of 185.3 million average common shares outstanding, compared with 12 cents on 134.7 million average common shares in 1986. The large increase in the number of outstanding common shares resulted from conversion of convertible preferred shares and warrants as the market price of the common shares increased during 1987.

The largest increase in net income was contributed by NOVA's petrochemical business which achieved higher sales volumes, reduced operating and manufacturing costs and improved prices. Cost-of-service income in gas transportation and petrochemical operations declined slightly due to lower rate bases and reduced returns in some operations. In petroleum, higher crude oil prices in upstream operations were offset by lower margins from downstream operations and lower natural gas prices.

The return on average common equity was 13.3% in 1987.

1986 Compared to 1985

Consolidated income before extraordinary items was $108.0 million, down from $134.1 million in 1985. Improved earnings in petrochemicals through better prices and increased production of polyethylene were more than offset by the effect of lower crude oil prices; lower rates of return and rate bases for certain gas transportation operations; and a decline in contribution from the valve manufacturing operations.

As a result of writing down the portion of NOVA's investment in Husky held for sale to net realizable value, an extraordinary loss of $7.8 million reduced consolidated net income for 1986 to $100.2 million or 12 cents per common share fully diluted.

In 1985 extraordinary items of $216.5 million

(Millions of dollars)

Year Ended December 31	1987	1986	1985
Revenue			
Gas Transportation & Marketing	$1,167.6	$1,245.4	$1,529.9
Petrochemicals	1,021.4	724.8	756.8
Petroleum	49.9	626.2	978.9
Manufacturing	103.5	105.9	97.4
Intersegment Eliminations	(20.0)	(21.3)	(15.8)
	$2,322.4	$2,681.0	$3,347.2
Operating Income			
Gas Transportation & Marketing	$ 320.2	$ 338.7	$ 345.5
Petrochemicals	202.9	73.6	48.1
Petroleum	(2.3)	158.2	266.5
Manufacturing	7.4	2.7	13.5
	$ 528.2	$ 573.2	$ 673.6

caused NOVA to report a net consolidated loss of $82.4 million or $1.31 per common share fully diluted.

Revenue and Operating Income

Significant trends in revenue and operating income are illustrated above and discussed by major business segment as follows.

Gas Transportation & Marketing

Revenue was down 6% in 1987 due to lower prices for natural gas marketed to the United States. The marketing of natural gas has little impact on operating income since the margins in this business yield only a small profit contribution. Lower rates of return and declining rate bases combined with reduced billings for income taxes and carrying costs related to the capital structure of certain cost-of-service operations caused the decline of 5% or $18.5 million in operating income. These factors reduced earnings attributable to common shareholders by $2.2 million.

1986 Compared to 1985

Revenue was down 19% due to lower prices and reduced volumes of natural gas marketed to the United States. Lower rates of return and declining rate bases in certain cost-of-service operations caused a decline of $6.8 million or 2% in operating income.

Petrochemicals

Revenue was up $296.6 million or 41% in 1987 due to increased volumes and improved prices in NOVA's polyethylene business. At the Joffre linear low-density polyethylene plant, sales volumes increased by 35% and average selling prices were up 23%. New revenue was contributed from the linear low/high-density polyethylene plant near Sarnia, Ontario, which was acquired in mid-February 1987.

Operating income was up $129.3 million, more than double the amount reported in 1986. The polyethylene business contributed most of this increase with higher sales volume and improved selling prices combined with reduced operating and manufacturing costs. The contribution from the Corporation's methanol business, which is discussed under equity in earnings (losses) of affiliated companies, also improved in 1987.

1986 Compared to 1985

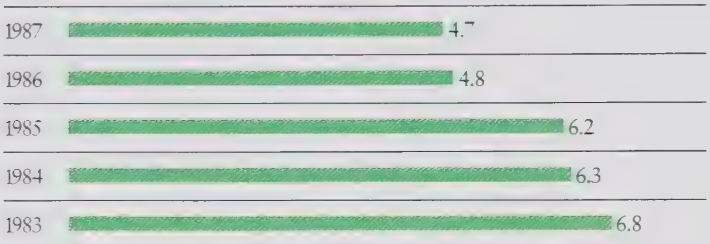
Revenue was down $32.0 million or 4%. The increased revenue for polyethylene was more than offset by reduced by-product sales from the ethylene plants as well as reduced price and demand for ethane. While revenue was down slightly in 1986 compared with 1985, operating income in 1986 improved by $25.5 million or 53% over 1985 due to improved prices and higher volumes for polyethylene.

Petroleum

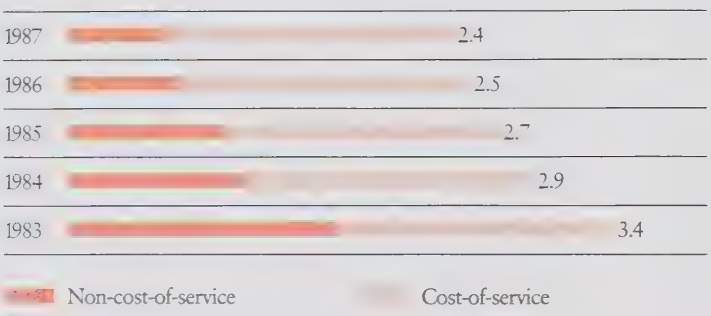
In 1987 NOVA's investment in Husky has been accounted for under the equity basis of accounting. Under this method NOVA's share of Husky's income is included as equity in earnings of affiliates. In 1986 NOVA consolidated Husky's accounts for eleven months and accordingly included in the 1986 revenue and operating income figures are

Net income increased by 79% in 1987 as NOVA's petrochemical business benefited from a strong recovery in operating and marketing conditions

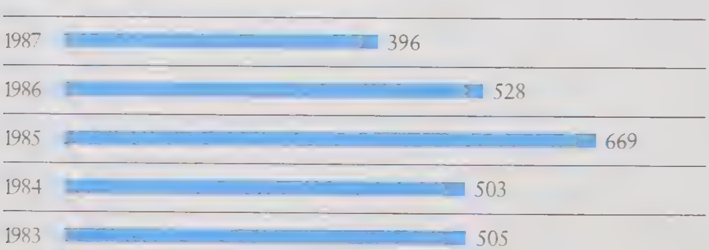
CONSOLIDATED ASSETS AT YEAR END
(Billions of dollars)



CONSOLIDATED LONG TERM DEBT AT YEAR END
(Billions of dollars)



CASH FROM OPERATIONS FOR THE YEAR
(Millions of dollars)



$591.9 million and $162.6 million respectively related to Husky.

The remaining petroleum investments consist of Novalta Resources, a wholly owned intermediate oil and gas company, and NOVA's consulting and engineering business. Novalta Resources maintained 1986 revenue levels despite the drop in natural gas prices; however, higher depletion charges, the result of increased production, reduced the net contribution. The consulting and engineering business, which had a $15.6 million increase in revenue from several new contracts, reported a small loss in both 1987 and 1986.

1986 Compared to 1985

Revenue was down 36% and operating income was down 41% principally due to the significant decrease in oil prices in the year. Lower volumes were experienced in the production of light and medium crudes which was a result of market and pipeline constraints.

Petroleum and gas revenue tax ("PGRT") decreased $78.5 million in 1986 due to the lower production volumes and selling price for crude oil. In addition, an agreement was reached by Husky during 1986 which resulted in PGRT exemptions and recoveries of $36.0 million.

Manufacturing

Revenue of $103.5 million remained relatively unchanged compared with 1986. Improved margins and reduced operating costs contributed to a $4.7 million improvement in operating income.

1986 Compared to 1985

Revenue in 1986 was up 9% compared with 1985; however, operating income declined 80%. The effect of lower crude oil prices contributed to substantial declines in oilfield-related activities and in turn to the decline in product margins in the valve group of companies, which are largely dependent on oil and gas activities.

Interest

Net interest expense was down 15% compared with 1986 due to a lower level of outstanding debt, arising principally from the proceeds received in May 1987 on the disposition of a part of the Husky investment, and lower levels of interest rates generally.

1986 Compared to 1985

Net interest expense was down 10% compared with 1985 due to a lower level of outstanding debt arising from the application of the proceeds received on the sale of NOVA's head office building.

Equity in Earnings (Losses) of Affiliated Companies

NOVA's share in earnings (losses) of affiliates, before non-operating items, was $12.8 million compared with a loss of $15.2 million in 1986. Most of the increase came from NOVA's investment in Husky which contributed $22.1 million ($14.4 million after interest of others in income of subsidiaries) in 1987. Husky benefited from higher crude oil prices but this was offset by lower margins in refining and marketing. In 1986 NOVA equity accounted for Husky for only one month and its contribution was $2.4 million. Earnings from NOVA's investment in the methanol business of $2.9 million were up $5.5 million, the result of increased sales volumes and reduced manufacturing costs. Methanol prices strengthened in the latter part of 1987 and this is expected to continue into 1988. Losses from manufacturing affiliates of $12.2 million improved by $2.8 million in the year. Losses are still being experienced in NOVA's telecommunication investment.

1986 Compared to 1985

NOVA's share in losses of affiliates in petrochemicals and manufacturing was $17.6 million in 1986 compared with $7.2 million in 1985. World methanol markets were depressed while the demand for heavy trucks remained weak. NOVA's telecommunication investment continued to face stiff competition in the cellular telephone market and lower crude oil prices significantly affected the marketing of compressed natural gas conversion equipment. Equity earnings from Husky were $2.4 million in 1986.

Loss on Investments

In 1987 NOVA recorded a net gain of $10.0 million on the sale of investments and recorded a net loss of $3.7 million on the sale of supply vessels. In addition NOVA discontinued the business of CNG Fuel Systems. The write-down of the investment resulted in a net loss of $21.7 million.

1986 Compared to 1985

In 1986 NOVA recorded its share of certain non-operating expenses incurred by affiliates accounted for by the equity method. These consisted of a $23.1 million loss in Husky, related to the write-downs of certain Canadian frontier and international oil and gas properties and a loss on the sale of a semi-submersible drilling vessel, and a loss of $7.0 million on the sale of a methanol plant in New Zealand.

Miscellaneous Income and Other (Deductions)

The increase in other expenses during 1987 and 1986 compared with 1985 is mainly due to rent for NOVA's head office building which was sold and leased back in December 1985.

Income Taxes

Income tax expense was up $12.7 million compared with 1986 principally as a result of higher earnings in petrochemical operations as offset by $35.7 million on the utilization of losses for tax purposes. The 1986 figure includes income taxes of $32.7 million provided by Husky.

1986 Compared to 1985

Income tax expense was down $94.3 million compared with 1985 principally as a result of lower earnings in the petroleum operations. Income tax expense for 1986 was reduced by $34.8 million by applying losses for tax purposes to income on which taxes had been previously paid or provided.

Liquidity and Capital Resources

Cash flow from operating activities totalled $395.6 million in 1987. After removing the effect of Husky ($223.0 million) from the 1986 figure of $527.9 million, the 1987 cash flow from ongoing consolidated operations was up $90.7 million. This improvement came principally from the petrochemical business.

Investment activities resulted in a net cash outflow of $146.6 million in 1987, down $47.1 million from 1986. Capital expenditures on plant, property and equipment were down $126.6 million principally as a result of the deconsolidation of Husky, which had capital expenditures of $173.0 million in the comparative period of 1986. NOVA's consolidated capital expenditure program for 1988 is currently estimated to be about

$350.0 million with $250.0 million of this related to expansion and improvement to the Alberta Gas Transmission Division gas gathering and delivery system.

In May 1987 NOVA received $359.0 million on the completion of the sale of a portion of its investment in Husky. In December 1987, as a result of improved long term opportunities, NOVA acquired, for about $215.2 million, additional common shares of Oil Term Holdings Ltd. ("Holdings"), a company whose only asset consists of a 43% interest in the common shares of Husky. As a result of the purchase NOVA became the beneficial owner of approximately 99% of Holdings and increased its indirect ownership of Husky common shares from 24.4% to 42.5%.

Financing activities in 1987 included the issuance of $31.2 million in common shares, $218.2 million of long term debt and the agreement to issue $150.0 million of convertible debentures in early 1988. Repayment of long term debt amounted to $118.1 million and the purchase of preferred shares (both the Corporation's and those of subsidiaries) amounted to $215.0 million. Dividends paid to common and preferred shareholders of the Corporation amounted to $126.3 million compared with $138.5 million in 1986.

At December 31, 1987, NOVA had consolidated working capital amounting to $79.8 million compared with $324.8 million in 1986. Included in working capital at the end of 1986 was $359.0 million representing the anticipated cash proceeds from the sale of a portion of the Husky investment which were received on May 1, 1987.

During 1987 common equity of the Corporation increased to $1.3 billion, almost double the 1986 figure, as a result of the conversion of preferred shares, the exercise of warrants, the issue of convertible debentures and improved earnings. The common equity per common share at year end increased to $5.76 from $4.22 at the end of 1986.

NOVA has access to additional credit facilities with several Canadian chartered banks. These are subject to routine review and, based on current discussions with NOVA's banks and other lenders, additional credit facilities would be available if required.

1986 Compared to 1985

Cash flow from operating activities totalled $527.9 million in 1986, down $141.5 million principally due to reduced petroleum results.

Investment activities resulted in a net cash outflow of $193.6 million in 1986, down $248.1 million from 1985. Expenditures on plant, property and equipment were down $60.9 million principally as a result of a planned reduction in production development activities which was implemented by Husky in late 1985 and early 1986 in anticipation of low crude oil prices. As well NOVA received $157.5 million in 1986 on the sale of its head office building.

Financing activities in 1986 included the issuance of $97.9 million of warrants and common shares of the Corporation as well as $100.2 million in additions to long term debt. Repayments of bank indebtedness and long term debt amounted to $328.5 million. Dividends paid to shareholders of the Corporation amounted to $138.5 million.

At December 31, 1986, NOVA had consolidated working capital amounting to $324.8 million compared with $33.0 million at the end of 1985. Included in working capital at the end of 1986 was $359.0 million representing the anticipated cash proceeds from the sale of a portion of the Husky investment.

Consolidated assets of NOVA at the end of 1986 were $4.8 billion, down from $6.2 billion in 1985 due to the effect of the deconsolidation of Husky.

NOVA Corporation of Alberta

Annual

Report

1987

Financial

Report

Management's Statement of Financial Reporting

The December 31, 1987 consolidated financial statements of NOVA Corporation of Alberta presented in the Annual Report have been prepared by management on a consistent basis in accordance with accounting principles generally accepted in Canada. The consolidated financial statements have been prepared within reasonable limits of materiality and within the framework of the accounting policies as outlined in the consolidated financial statements. The financial information contained elsewhere in this Annual Report is consistent with that in the consolidated financial statements.

The Corporation maintains systems of internal accounting controls, policies and procedures to provide assurance as to the reliability of the financial information and the protection of assets.

Clarkson Gordon, the Corporation's independent auditors, have examined the December 31, 1987 consolidated financial statements and their report follows.

The Audit Committee of your Board of Directors, comprising directors who are not employees of the Corporation, has reviewed the consolidated financial statements, including the notes thereto, with management and the independent auditors. The consolidated financial statements have been approved by your Board of Directors on the recommendation of the Audit Committee.

Auditors' Report

To the Shareholders of
NOVA Corporation of Alberta
(formerly NOVA, AN ALBERTA CORPORATION)

We have examined the consolidated balance sheet of NOVA Corporation of Alberta as at December 31, 1987 and 1986 and the consolidated statements of income, reinvested earnings, contributed surplus and changes in financial position for each of the years in the three year period ended December 31, 1987. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1987 and 1986 and the results of its operations and the changes in its financial position for each of the years in the three year period ended December 31, 1987 in accordance with accounting principles generally accepted in Canada applied on a consistent basis.

Clarkson Gordon

Chartered Accountants

Calgary, Canada
February 22, 1988

CONSOLIDATED STATEMENT OF INCOME

(Thousands of dollars except for share data)

Year Ended December 31	1987	1986	1985
Revenue	$2,322,438	$2,680,966	$3,347,236
Operating Costs and Expenses			
Operating expenses	1,603,201	1,819,347	2,288,419
Depreciation and depletion	178,071	292,544	310,180
Petroleum and gas revenue tax	–	(25,620)	52,903
Loss on foreign currency translation	12,968	21,474	22,162
	1,794,240	2,107,745	2,673,664
Operating Income	528,198	573,221	673,572
Other Income (Deductions)			
Interest expense (Note 9)	(242,729)	(284,292)	(315,915)
Allowance for funds used during construction	2,501	3,480	3,171
Equity in earnings (losses) of affiliates	12,789	(15,204)	(7,235)
Loss on investments (Note 13)	(18,146)	(30,125)	–
Miscellaneous income and other (deductions)	(13,410)	(14,312)	1,921
	(258,995)	(340,453)	(318,058)
Income Before Income Taxes, Interest of Others in Income of Subsidiaries and Extraordinary Items	269,203	232,768	355,514
Income Taxes (Note 14)	(74,341)	(61,614)	(155,892)
Interest of Others in Income of Subsidiaries	(15,732)	(63,157)	(65,511)
Income Before Extraordinary Items	179,130	107,997	134,111
Extraordinary Items (Note 15)	–	(7,800)	(216,522)
Net Income (Loss)	179,130	100,197	(82,411)
Less Preferred Share Dividend Entitlement	49,296	84,071	85,511
Net Income (Loss) to Common Shareholders	$ 129,834	$ 16,126	$ (167,922)
Average Common Shares Outstanding (Thousands)	185,321	134,655	128,087
Net Income (Loss) Per Common Share			
Before extraordinary items			
Basic	$ 0.70	$ 0.18	$ 0.38
Fully diluted	$ 0.67	$ 0.17	$ 0.38
After extraordinary items			
Basic	$ 0.70	$ 0.12	$ (1.31)
Fully diluted	$ 0.67	$ 0.12	$ (1.31)

See accompanying summary of accounting policies and notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEET

ASSETS		(Thousands of dollars)
December 31	1987	1986
Current Assets		
Cash and short term deposits	$ 74,207	$ 48,407
Funds on deposit	–	138,050
Receivables (Note 3)	405,449	300,428
Inventories (Note 4)	117,354	110,441
Asset held for sale (Note 5)	–	358,998
Prepaid expenses	8,004	6,931
	605,014	963,255
Long Term Investments (Note 5)	768,308	505,318
Plant, Property and Equipment (Note 6)	4,455,908	4,282,265
Less accumulated depreciation and depletion	1,227,425	1,064,734
	3,228,483	3,217,531
Other Assets (Note 7)	83,943	76,848
	$4,685,748	$4,762,952

On behalf of the Board:

Director

Director

See accompanying summary of accounting policies and notes to consolidated financial statements.

Liabilities and Common Shareholders' Equity

December 31	1987	1986
		(Thousands of dollars)
Current Liabilities		
Bank loans (Note 9)	$ 72,163	$ 76,986
16-1/4% Unsecured debentures	–	138,050
Accounts payable and accrued liabilities (Note 8)	342,879	312,361
Income taxes payable	4,044	6,022
Dividends payable	29,813	35,186
Long term debt instalments due within one year (Note 9)	76,290	69,884
	525,189	638,489
Long Term Debt (Note 9)	2,358,941	2,390,999
Deferred Income Taxes	103,532	53,583
Deferred Gain	52,879	57,535
Interest of Others in Subsidiaries	13,502	146,731
Preferred Shares–Redeemable (Notes 1 and 10)	328,908	826,908
Convertible Debentures and Common Shareholders' Equity		
Convertible debentures (Note 11)	150,000	–
Common shareholders' equity		
Common shares and warrants (Notes 1 and 12)	774,430	323,406
Cumulative translation adjustment	21,323	19,800
Reinvested earnings	357,044	77,351
Contributed surplus	–	228,150
	1,302,797	648,707
Contingencies and Commitments (Note 18)		
	$4,685,748	$4,762,952

CONSOLIDATED STATEMENT OF REINVESTED EARNINGS

			(Thousands of dollars)
Year Ended December 31	1987	1986	1985
Beginning of year	$ 77,351	$115,676	$336,342
Net income (loss)	179,130	100,197	(82,411)
Transfer from contributed surplus (Note 1)	226,868	—	—
	483,349	215,873	253,931
Less dividends			
Preferred shares	49,296	84,071	86,636
Common shares	77,009	54,451	51,619
	126,305	138,522	138,255
End of year	$357,044	$ 77,351	$115,676

CONSOLIDATED STATEMENT OF CONTRIBUTED SURPLUS

			(Thousands of dollars)
Year Ended December 31	1987	1986	1985
Beginning of year	$228,150	$227,943	$228,171
Gain (loss) on preferred shares redeemed or purchased for cancellation	(1,282)	1,846	1,445
Capital stock and warrants issue expenses less income taxes	—	(1,639)	(1,673)
Transfer to reinvested earnings (Note 1)	(226,868)	—	—
End of year	$ —	$228,150	$227,943

See accompanying summary of accounting policies and notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
Operating Activities			
Income before extraordinary items	**$179,130**	$107,997	$134,111
Depreciation and depletion	**178,071**	292,544	310,180
Deferred income taxes	**67,347**	34,632	80,552
Interest of others in income of subsidiaries	**15,732**	63,157	65,511
Equity in (earnings) losses of affiliates	**(12,789)**	15,204	7,235
Loss on investments	**18,146**	30,125	–
Other	**32,106**	3,628	12,177
Changes in non-cash working capital (Note 16)	**(82,102)**	(19,345)	59,627
	395,641	527,942	669,393
Investment Activities			
Proceeds on sale of investments	**358,998**	157,500	14,098
Plant, property and equipment	**(199,796)**	(326,375)	(387,318)
Purchase of the interest of others in subsidiary (Note 5)	**(215,153)**	–	–
Other assets and long term investments	**(101,843)**	(44,010)	(48,185)
Other	**3,317**	3,373	3,262
Changes in non-cash working capital (Note 16)	**7,921**	15,894	(23,571)
	(146,556)	(193,618)	(441,714)
Financing Activities			
Preferred shares issued	**–**	–	96,844
Warrants issued	**–**	71,800	–
Common shares issued	**31,184**	26,089	27,540
Long term debt additions	**218,235**	100,189	123,788
Bank indebtedness and long term debt repaid	**(118,141)**	(328,512)	(234,271)
Preferred shares purchased for cancellation	**(79,433)**	(16,034)	(12,318)
Preferred shares of subsidiaries redeemed	**(135,576)**	(28,876)	(25,725)
Dividends—to shareholders of the Corporation	**(126,305)**	(138,522)	(138,255)
—to other shareholders of partially owned subsidiaries	**(7,876)**	(17,599)	(30,064)
Changes in non-cash working capital (Note 16)	**(5,373)**	772	2,488
	(223,285)	(330,693)	(189,973)
Increase in Cash Position	**25,800**	3,631	37,706
Cash Position at Beginning of Year	**48,407**	44,776	7,070
Cash Position at End of Year	**$ 74,207**	$ 48,407	$ 44,776

See accompanying summary of accounting policies and notes to consolidated financial statements.

The consolidated financial statements have been prepared on the historical cost basis in accordance with accounting principles generally accepted in Canada. The significant accounting policies are as follows:

Principles of consolidation

The consolidated financial statements include the accounts of NOVA Corporation of Alberta (the "Corporation"), its subsidiaries and the proportionate share of assets, liabilities, revenues and expenses of certain of its gas transportation and marketing and petrochemical investments.

Cost of service

Some gas transportation and marketing and petrochemical operations are subject to cost-of-service agreements. Such agreements, as approved by governmental or regulatory bodies, provide for the recovery of reasonable and necessary operating expenses, cost of feedstock and fuel, depreciation, amortization, income and other taxes, foreign exchange losses in respect of debt service and a rate of return on investment.

Foreign currency translation

Foreign operations which are considered financially and operationally independent have been translated to Canadian dollars using the year-end rate of exchange (the "current rate") for assets and liabilities and average rates for the year for revenues and expenses. Gains or losses resulting from these translation adjustments are deferred in a separate component of common shareholders' equity (the "Cumulative Translation Adjustment" account) until there is a realized reduction of the investment in the foreign operation.

Foreign denominated long term monetary items (principally long term debt) of Canadian operations are translated at the current rate of exchange. For foreign denominated long term monetary items of cost-of-service operations, the exchange differential is recoverable from customers and is reported as a reduction in the associated long term monetary item. The unrealized translation gains or losses related to non-cost-of-service operations are deferred and are amortized over the remaining lives of the long term monetary items.

Inventories

Inventories are carried at the lower of cost determined on a first-in, first-out basis and net realizable value.

Investments

The Corporation accounts for its investments in affiliates by the equity method. Under this method, the investment is carried at cost plus the related share of undistributed earnings less the amortization of the excess of the purchase price over the net book value at date of acquisition. Notes receivable and other investments are carried at cost.

Plant, property and equipment

Plant, property and equipment are carried at cost and additions include related financing costs during major plant construction.

The Corporation's investments in petroleum are accounted for under the full cost method of accounting whereby all costs of acquiring properties, exploring for and developing oil, natural gas and sulphur and related reserves are capitalized and accumulated in country-by-country cost centres. Such costs include land acquisition, drilling both productive and non-productive wells, overhead expenses and financing. The net carrying amount of each cost centre is limited to a ceiling test amount which is the estimated future net revenues from proved reserves (based on current prices and costs at the balance sheet date) plus unproved properties at cost less an allowance for impairment. The total capitalized costs less depletion and depreciation and deferred income taxes of all cost centres are further limited to the aggregate estimated future net revenues for all cost centres less recurring general and administrative costs, future financing costs and income taxes. Any costs carried on the balance sheet in excess of these ceiling test amounts are charged to income.

Depreciation and depletion

Plant and equipment are depreciated at annual rates varying from 3-1/2% to 33-1/3% which rates are designed to write these assets off over their estimated useful lives.

For oil and natural gas operations, depletion and depreciation is provided on the unit of production method based on gross proved reserves in each cost centre. Reserves are converted to equivalent units on the basis of approximate relative energy content. Costs of acquiring and evaluating unproved properties are excluded from the calculation of depletion and depreciation until it is determined that proved reserves are attributable to the properties or that impairment has occurred.

Allowance for funds used during construction

For some gas transportation and marketing and petrochemical operations, a return on capital invested in new plant while under construction, which is recoverable from customers, has been included in income.

Income taxes

The deferral method of tax allocation accounting is followed in respect of all income except for some gas transportation and marketing and petrochemical operations which are subject to cost-of-service agreements. Under this method, provision is made for income taxes deferred principally as a result of claiming capital cost allowance and exploration and development costs for income tax purposes in excess of depreciation and depletion provided in the accounts. The agreements for certain cost-of-service operations provide for the recovery of income taxes on the taxes payable method. Thus the income tax provision recorded for these operations represents only the income taxes deemed to be currently payable and thus recoverable under the billing mechanism in place. Investment tax credits are recorded as a reduction in the cost of the related asset.

Deferred gain

The gain realized from the sale and leaseback of the Corporation's head office building in 1985 has been deferred and is being credited to income over the term of the lease.

Pension plans

The cost of pension benefits earned by employees is determined using the projected benefit method prorated on service and is charged to expense as services are rendered in all operations except for those which are subject to cost-of-service agreements. The cost of pension benefits reflects management's best estimates of the expected investment yields, salary escalations, mortality rates, terminations and the age at which members will retire. Adjustments arising from plan amendments, experience gains and losses, and changes in assumptions are amortized on a straight-line basis over the estimated average remaining service lives of the employee groups.

The agreements for certain cost-of-service operations provide for the recovery of pension costs on the basis of cash contributions. Thus the pension expense represents only contributions made to the pension plans during the year and therefore recoverable under the billing mechanism in place.

Net income per common share

Basic net income per common share is calculated using the weighted average number of common shares outstanding during the respective year and after provision for preferred share dividend entitlement. The calculation of net income per common share on a fully diluted basis assumes conversion of all securities and exercise of all common share purchase warrants or options if such action would result in dilution of income per common share.

Comparative figures

Certain comparative figures for the years ended December 31, 1986 and 1985, have been reclassified to conform to the current year's financial statement presentation.

1. Restructuring of the Corporation

On September 1, 1987, the Corporation was restructured pursuant to the Business Corporations Act of Alberta and the name of the Corporation was changed to NOVA Corporation of Alberta.

At that time the Corporation redeemed its Class "B" common shares at their par value and reorganized its remaining share capital into several classes of shares, being First Preferred Shares, Second Preferred Shares, Junior Preferred Shares, Subordinated Junior Preferred Shares and Common Shares (formerly the Class "A" common shares).

Pursuant to a resolution of its Board of Directors and in anticipation of the reorganization of its share capital, the Corporation on August 31, 1987, transferred the balance in the contributed surplus account to reinvested earnings.

2. Proportionate Consolidation of Certain of the Corporation's Investments

The Corporation has proportionately consolidated some of its gas transportation and marketing and petrochemical investments. The components of the Corporation's consolidated balance sheet and consolidated statement of income relating to its share of the activities of these investments are shown below:

(Thousands of dollars)

Year Ended December 31	Assets	Liabilities	Revenue	Operating Costs and Expenses
Gas Transportation & Marketing				
1987	$694,138	$478,792	$131,899	$ 47,869
1986	706,082	478,417	143,764	50,269
1985	732,466	495,623	151,840	49,491
Petrochemicals				
1987	140,788	87,081	65,003	50,418
1986	141,932	90,230	60,185	49,291
1985	153,640	98,526	89,502	76,258
Totals				
1987	$834,926	$565,873	$196,902	$ 98,287
1986	848,014	568,647	203,949	99,560
1985	886,106	594,149	241,342	125,749

3. Receivables

(Thousands of dollars)

December 31	1987	1986
Trade	$331,667	$230,338
Other	74,748	70,572
	406,415	300,910
Less allowance for doubtful accounts	966	482
	$405,449	$300,428

4. Inventories

December 31	1987	1986
	(Thousands of dollars)	
Materials and supplies	$ 46,650	$ 44,897
Raw materials	22,354	26,251
Work in process	12,474	10,885
Finished goods	29,645	18,245
Other	6,231	10,163
	$117,354	$110,441

5. Long Term Investments

December 31	1987	1986
	(Thousands of dollars)	
Alberta Gas Chemicals Ltd. (50% owned)	$ 12,817	$ 9,941
CNG Fuel Systems (Note 13)	–	20,341
Husky Oil Ltd.	581,204	344,149
NovAtel Communications Ltd. (50% owned)	55,712	70,095
Polysar Energy & Chemical Corporation (Note 20)	72,225	–
Western Star Trucks Inc. (50% owned)	6,854	13,083
Notes receivable and other investments	39,496	47,709
	$768,308	$505,318

On April 30, 1987, the reorganization of Husky Oil Ltd. ("Husky") was completed. As a result the Corporation received $358,998,000 on May 1, 1987, reduced its interest in Husky common shares from 56.7% to 24.4% and received Husky Class "C" preferred shares. The Corporation's interest in preferred and common shares of Husky is held through two holding companies, Oil Term Investment Ltd. ("Investment") and Oil Term Holdings Ltd. ("Holdings").

The Corporation owns 97.8% of Investment which in turn owns 57.9% of Holdings. Holdings owns 43% of Husky common shares. On December 31, 1987, the Corporation acquired the 42.1% of Holdings not owned by Investment for $215,153,000. As a result of this acquisition the Corporation's interest in Husky common shares increased from 24.4% to 42.5%.

Investment also owns 100% of the Husky Class "C" preferred shares which are redeemable at any time prior to April 30, 1992, for $81,000,000. After April 30, 1992, the Class "C" preferred shares are redeemable for a minimum of $54,000,000 to a maximum of $81,000,000 plus interest and are retractable for cash or an interest in certain frontier and heavy oil properties.

The Corporation consolidated the accounts of Husky to November 30, 1986, thereafter the Corporation's indirect 24.4% interest has been accounted for by the equity basis.

The following sets out summarized financial information for Husky:

December 31	1987	1986	1985
			(Thousands of dollars)
Current assets	$ 320,961	$ 276,849	$ 411,249
Long term investments	19,362	27,768	25,716
Plant, property and equipment	1,395,480	1,403,539	1,541,384
Other assets	2,636	8,047	11,106
Current liabilities	(227,454)	(221,271)	(396,332)
Long term debt	(119,654)	(172,472)	(224,892)
Deferred income taxes	(333,812)	(309,037)	(369,217)
Shareholders' equity	$1,057,519	$1,013,423	$ 999,014

Year Ended December 31	1987	1986	1985
			(Thousands of dollars)
Revenue	$ 571,887	$ 637,662	$ 923,277
Operating costs and expenses	(449,758)	(465,345)	(641,504)
Interest expense	(9,427)	(7,238)	(20,118)
Gain (loss) on investments*	8,893	(182,954)	—
Income taxes	(50,865)	54,280	(135,670)
Net income	$ 70,730	$ 36,405	$ 125,985

*In 1987 Husky recorded a gain of $35,598,000 ($26,423,000 after income taxes) on the sale of investments and a loss of $26,705,000 ($15,005,000 after income taxes) on the sale of its supply vessels. In 1986 Husky incurred a loss of $154,634,000 ($78,704,000 after income taxes) on the write-down of the carrying value of certain Canadian frontier and international oil and gas properties and a loss of $28,320,000 ($15,960,000 after income taxes) on the sale of a semi-submersible drilling rig (see Note 13).

6. Plant, Property and Equipment

(Thousands of dollars)

December 31	1987			1986
	Cost	Accumulated Depreciation and Depletion	Net	Net
Gas Transportation & Marketing	$2,770,600	$ 761,956	$2,008,644	$2,023,633
Petrochemicals	1,323,752	351,440	972,312	951,921
Petroleum—full cost method	223,093	58,086	165,007	162,561
Manufacturing and other	138,463	55,943	82,520	79,416
	$4,455,908	$1,227,425	$3,228,483	$3,217,531

7. Other Assets

(Thousands of dollars)

December 31	1987	1986
Deferred project costs	$ —	$ 9,448
Unamortized debt discount and expense	16,067	10,868
Unamortized foreign exchange translation adjustments	67,876	56,532
	$ 83,943	$ 76,848

8. Accounts Payable and Accrued Liabilities

	(Thousands of dollars)	
December 31	1987	1986
Accounts payable		
Trade	$ 232,419	$ 156,051
Other	13,291	10,193
	245,710	166,244
Accrued liabilities		
Interest	53,020	76,148
Other	44,149	69,969
	97,169	146,117
	$ 342,879	$ 312,361

9. Long Term Debt

Related to Cost-of-Service Operations

Represents long term debt in operations which are subject to cost-of-service or tariff agreements under which realized foreign exchange gains or losses are for the account of the customer.

		(Thousands of dollars)	
December 31	Maturity	1987	1986
NOVA Corporation of Alberta			
Alberta Gas Transmission Division			
Unsecured Debentures			
9-3/4% Series 2	1990	$ 12,783	$ 14,071
9-1/4% Series 3	1990	11,479	12,729
8% Series 4	1991	34,561	36,409
8-1/8% Series 5	1992	25,866	26,301
11-3/8% Series 6	1995	40,953	45,986
17-1/2% Series 7		–	75,000
17-3/4% Series 8	1997	42,500	45,000
12-1/8% Series 9	1993	100,000	100,000
11-1/8% Series 12	1993	50,000	–
11.95% Series 13	2007	125,000	–
10% Series B	1996	100,000	100,000
8-3/4% Series C (1987 and 1986 - U.S. $100,000)	1994	129,930	138,050
Unsecured Term Notes			
9.65% (1987 - U.S. $35,000)	1992	45,475	–
9.95% (1987 - U.S. $75,000)	1995	97,448	–
16-1/8% - average (1986 - U.S. $110,000)		–	151,855
Other Loans* (1987 - U.S. $11,220; 1986 - U.S. $16,180)	1989	14,577	22,336
		830,572	767,737
Less exchange differential recoverable from cost-of-service customers		18,411	37,899
		812,161	729,838

December 31	Maturity	1987	1986
		(Thousands of dollars)	
Foothills (Yukon)—Phase I			
Secured Loans*	1996	$ 227,885	$ 242,149
TQM Pipeline			
First Mortgage Bonds			
13.10% Series A	1994	50,000	50,000
13.20% Series B	2004	50,000	50,000
11.70% Series C	1990	42,500	42,500
Secured Loan*	1990	7,001	19,167
		149,501	161,667
Alberta Gas Ethylene			
Ethylene Plant I			
8-1/4% Secured Notes (1987-U.S. $156,923; 1986-U.S. $171,188)	1998	203,890	236,325
Ethylene Plant II			
Secured Loan* (1987-U.S. $220,173; 1986-U.S. $233,450)	2004	286,071	322,278
Secured Notes			
13-3/4% Series A (1987-U.S. $36,458; 1986-U.S. $41,458)	2004	47,370	57,233
9.85% Series B (1987-U.S. $25,500; 1986-U.S. $27,000)	2004	33,132	37,274
Secured Bank Loan*	1991	3,919	–
		574,382	653,110
Less exchange differential recoverable from cost-of-service customers		35,232	76,596
		539,150	576,514
Other Loans*	Various	59,261	52,990
Total Related to Cost-of-Service Operations		1,787,958	1,763,158
Related to Non-Cost-of-Service Operations			
NOVA Corporation of Alberta			
Unsecured Debentures			
14% Series 10	1989	100,000	100,000
12% Series 11	1990	125,000	125,000
Unsecured Term Notes			
6-1/4% (1987 and 1986—Swiss Francs 175,000,000)	1991-1992	179,043	150,010
Unsecured Bank Loans and Notes*		273,219	209,137
Less convertible debentures (Note 11)		(150,000)	–
		527,262	584,147
Novalta Resources			
Income Debentures*			
(1987 - U.S. $21,258; 1986 - U.S. $24,686)	1988-1989	27,621	34,079
Other Loans*	Various	92,390	79,499
Total Related to Non-Cost-of-Service Operations		647,273	697,725
		2,435,231	2,460,883
Less instalments due within one year		76,290	69,884
		$2,358,941	$2,390,999

* *The interest rate is a function of generally prevailing money market interest rates, Canadian bank prime rates and London Inter Bank Offered Rates. The composite average interest rate for these loans at December 31, 1987 and 1986, was approximately 9-1/8%.*

In connection with various loans, security has been given as follows:

Foothills (Yukon) - Phase I

This financing is secured by the assignment of the interest of Foothills (Yukon) and three of its subsidiaries in certain agreements and floating charges on their respective properties and assets.

TQM Pipeline

The First Mortgage Bonds and the secured loan are secured by a first fixed and specific charge on the TQM Pipeline system, a pledge, charge and assignment of gas transportation service contracts and gas sales agreements and a floating charge on other property.

Alberta Gas Ethylene

Ethylene Plant I

The Secured Notes are secured by a first fixed and floating charge on the first ethylene plant, the ethylene pipeline and related assets of Alberta Gas Ethylene and by the assignment of certain related contracts.

Ethylene Plant II

This financing is secured by charges on certain of the proceeds of the ethylene sales contracts for the second ethylene plant, charges on related performance guarantees and a first fixed charge on the second ethylene plant and certain related agreements.

Novalta Resources

Security for the Income Debentures includes natural gas properties and a general assignment of book debts.

Other Loans

Other loans of $166,228,000 at December 31, 1987, ($154,825,000 at December 31, 1986) are secured by certain assets and agreements.

Sinking Fund and Repayment Requirements

Sinking fund and repayment requirements in respect to long term debt maturing within five years following December 31, 1987, are: 1988 - $76,290,000; 1989 - $187,145,000; 1990 - $278,698,000; 1991 - $173,298,000; 1992 - $238,791,000.

Current Bank Loans

Current bank loans of $72,163,000 at December 31, 1987, ($76,986,000 at December 31, 1986) include loans of $62,620,000 ($60,265,000 at December 31, 1986) which are secured by certain assets and agreements.

Lines of Credit

At December 31, 1987, the Corporation had committed credit facility agreements with several Canadian banks aggregating $750,000,000.

Interest Expense (Net)

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
Interest on long term debt	$244,576	$307,919	$336,648
Interest on short term debt	12,428	22,181	19,222
Interest capitalized	(2,064)	(26,510)	(18,839)
Interest income	(12,211)	(19,298)	(21,116)
	$242,729	$284,292	$315,915

10. Preferred Shares—Redeemable

(a) Authorized

Unlimited number of cumulative first, second and junior preferred shares without par value.

100,000,000 subordinated junior preferred shares without par value.

(b) Issued and Outstanding

		(Number of shares)			(Thousands of dollars)	
December 31	1987	1986	1985	1987	1986	1985
Related to Cost-of-Service Operations						
First preferred shares						
4-3/4% Series C	**42,071**	50,331	61,638	**$ 4,207**	$ 5,033	$ 6,164
7-3/4%	**650,871**	677,871	702,531	**16,272**	16,947	17,564
9-3/4%	**780,573**	792,939	971,091	**19,514**	19,824	24,277
9.76%	**1,196,778**	1,293,578	1,389,448	**29,919**	32,339	34,736
7.60%	**2,211,400**	2,302,800	2,394,200	**55,285**	57,570	59,855
15%	**–**	2,500,000	2,500,000	**–**	62,500	62,500
				125,197	194,213	205,096
Related to Non-Cost-of-Service Operations						
First preferred shares						
11.24%	**4,000,000**	4,000,000	4,000,000	**100,000**	100,000	100,000
9-1/8%	**3,997,700**	4,000,000	4,000,000	**99,943**	100,000	100,000
Second preferred shares						
6-3/8%	**150,733**	166,633	877,650	**3,768**	4,166	21,941
6-1/2%	**–**	6,946,004	7,200,525	**–**	173,650	180,013
12%	**–**	10,195,170	10,196,270	**–**	254,879	254,907
				203,711	632,695	656,861
				$328,908	$826,908	$861,957

(c) Commentary

The following is a summary of material characteristics of the issued and outstanding preferred shares:

Preferred Share Issue	Stock Exchange Symbol	Annual Dividend Per Share	Redemption Features	Sinking Fund and Purchase Fund Requirements (1)
4-3/4% Series C	C	$4.75	at $101.00 per share	purchase obligation of $825,000 annually, to the extent the shares are available at a price not in excess of $100.00 per share; any purchase deficiency must be satisfied by partial redemption at a price of $101.00 per share within 15 days in the following year
7-3/4%	E	$1.94	at $26.00 per share on or before May 15, 1989, and at reducing amounts thereafter	purchase obligation of $750,000 annually, to the extent the shares are available at a price not in excess of $25.00 per share; the purchase obligation is cumulative to a maximum of $1,500,000

Preferred Share Issue	Stock Exchange Symbol	Annual Dividend Per Share	Redemption Features	Sinking Fund and Purchase Fund Requirements (1)
9-3/4%	F	$2.44	at $25.00 per share	purchase 64,000 shares annually at a price not in excess of $25.00 per share by May 15 of each year under a cumulative mandatory sinking fund
9.76%	G	$2.44	at $25.00 per share	purchase 96,000 shares annually at a price not in excess of $25.00 per share by November 15 of each year under a cumulative mandatory sinking fund
7.60%	H	$1.90	at $25.25 per share on or before February 15, 1988, and at reducing amounts thereafter	purchase 90,000 shares annually at a price not in excess of $25.00 per share
11.24%	N	$2.81	at $26.25 per share on or after May 15, 1988, to May 15, 1989, and at reducing amounts thereafter; retractable on May 15, 1988, at $25.00 per share	purchase 80,000 shares annually at a price not in excess of $25.00 per share to May 15, 1988, and thereafter 4% of the outstanding balance on an annual basis
9-1/8% (2)	O	$2.28	at $25.00 per share on or after February 15, 1990; retractable on February 15, 1995, at $25.00 per share	purchase 3% of the shares outstanding annually, commencing February 16, 1995, at a price not in excess of $25.00 per share
6-3/8%	J	$1.59	at $25.25 per share on or before November 15, 1988, and at reducing amounts thereafter	purchase 216,000 shares annually at a price not in excess of $25.00 per share

(1) The Corporation must make all reasonable efforts to satisfy the sinking and purchase fund requirements at prices not in excess of the stated price per share plus accrued and unpaid dividends and costs of purchase. In addition to the cumulative mandatory sinking funds, the Corporation may call for redemption and redeem annually, through the operation of non-cumulative optional sinking funds, 48,000 9-3/4% Preferred Shares and 72,000 9.76% Preferred Shares at par value plus accrued and unpaid dividends.

The redemption requirements within the five years following December 31, 1987, are: 1988 - $15,874,000; 1989 - $11,665,000; 1990 - $11,511,000; 1991 -$11,364,000 and 1992 - $11,222,000.

(2) Commencing in 1990, the dividend payment on the 9-1/8% Preferred Shares will be equal to 70% of the average of the Canadian prime rate for the dividend period.

(d) Purchases

The Corporation purchased for redemption or cancellation 3,101,211 shares in 1987, 681,289 shares in 1986, and 520,335 shares in 1985.

11. Convertible Debentures

In mid-December 1987, the Corporation reached a definitive agreement to issue adjustable rate convertible subordinated debentures (the "Convertible Debentures") in the amount of $150,000,000. On January 11, 1988, the Convertible Debentures were issued and the proceeds were applied against unsecured bank loans and notes classified as long term debt at December 31, 1987. The Corporation has included the proceeds of the Convertible Debentures as a reduction in unsecured bank loans and notes classified as long term debt at December 31, 1987.

The Convertible Debentures, which are unsecured and mature on February 15, 2008, pay a minimum interest rate of 6-1/4%. They are convertible at the holder's option until February 15, 2008, into common shares of the Corporation at an initial conversion price of $10.70 per share, subject to adjustment in certain events, which equates to 14,018,692 common shares. The debentures are also redeemable at par after February 15, 1993, and at any time prior to this date, at 105% of par if at least 85% of the original principal amount of the debentures has been converted.

The Convertible Debentures have been reported under the heading "Convertible Debentures and Common Shareholders' Equity" on the balance sheet. At its option at maturity, the Corporation can issue common shares in respect of the principal amount of the outstanding debentures at then prevailing market prices. The Corporation anticipates that the Convertible Debentures will ultimately be converted into common shares.

12. Common Shares and Warrants

(a) Authorized

Unlimited number of voting common shares without par value.

5,000,000 warrants.

(b) Issued and Outstanding

	(Number of shares and warrants)			*(Thousands of dollars)*		
December 31	1987	1986	1985	1987	1986	1985
Common Shares	211,483,734	141,839,334	130,656,702	$770,606	$264,262	$205,140
Class "B" Common Shares	–	1,717	1,665	–	9	8
	211,483,734	141,841,051	130,658,367	770,606	264,271	205,148
Warrants	254,950	3,942,315	–	3,824	59,135	–
				$774,430	$323,406	$205,148

(c) Common Shares Issued

Changes in the common share capital for the three years ended December 31, 1987, are summarized as follows:

	(Thousands of dollars)	
	Number of Shares	Common Share Capital
December 31, 1984	125,251,870	$172,726
For cash under the Dividend Reinvestment and Share Purchase Plan	4,518,987	27,072
On conversion of–		
194,805 6-3/8% Preferred Shares	818,181	4,870
150 6-1/2% Preferred Shares	387	4
For cash on exercise of stock options (at prices ranging from $6.625 to $7.375)	67,277	468
	5,404,832	32,414
December 31, 1985	130,656,702	205,140
For cash under the Dividend Reinvestment and Share Purchase Plan	5,141,443	26,088
On conversion of–		
675,417 6-3/8% Preferred Shares	2,836,751	16,885
10,221 6-1/2% Preferred Shares	27,665	256
1,100 12% Preferred Shares	3,718	28
On exercise of 1,057,685 Warrants	3,173,055	15,865
	11,182,632	59,122
December 31, 1986	141,839,334	264,262
For cash under the Dividend Reinvestment and Share Purchase Plan	2,475,270	20,822
On conversion of–		
6,712,368 6-1/2% Preferred Shares	19,617,432	167,809
10,081,621 12% Preferred Shares	34,993,228	252,040
On exercise of 3,687,365 Warrants	11,062,095	55,311
For cash on exercise of stock options (at prices ranging from $4.85 to $8.75)	1,496,375	10,362
	69,644,400	506,344
December 31, 1987	211,483,734	$770,606

(d) Common Shares Reserved for Future Issue

		(Number of shares)
December 31	1987	1986
Under the Dividend Reinvestment and Share Purchase Plan	**6,094,909**	2,570,043
For conversion of 6-1/2% Preferred Shares	–	18,858,401
For conversion of 12% Preferred Shares	–	34,459,675
For exercise of Warrants	**764,850**	11,826,945
Under the Incentive Stock Option Plan (1982), options are outstanding to officers and employees to purchase 6,644,225 common shares at prices ranging from $4.85 to $10.375 per share (4,486,850 shares at December 31, 1986, at prices ranging from $4.85 to $7.375 per share) with expiration dates between 1988 to 1994, and 1,199,750 common shares are reserved but unallocated (403,500 shares at December 31, 1986)	**7,843,975**	4,890,350
	14,703,734	72,605,414

(e) Warrants

The Warrants were issued in 1986 at a price of $15.00 per Warrant. Each Warrant entitles the holder at his option to obtain on exercise three common shares at any time before July 31, 1996, or either one no par value first preferred share or one no par value second preferred share from August 1, 1991, to July 31, 1996. The Corporation may purchase for cancellation any or all of the Warrants outstanding in the market.

13. Loss on Investments

(a) For the Year Ended December 31, 1987

(Thousands of dollars)

	Per Statement Caption	Net Income Effect*
Gain on sale of investments	$ 16,004	$ 9,991
Loss by Husky on sale of supply vessels	(6,450)	(3,660)
Provision for loss on shutdown of CNG Fuel Systems	(27,700)	(21,700)
	$(18,146)	$(15,369)

* After income taxes and interest of others in income of subsidiaries.

(b) For the Year Ended December 31, 1986

Share of certain non-operating costs incurred by equity accounted affiliates:

Write-down by Husky of the carrying value of oil and gas properties	$(19,176)	$(19,176)
Loss by Husky on sale of semi-submersible drilling rig	(3,889)	(3,889)
Loss by Alberta Gas Chemicals on sale of New Zealand methanol plant interest	(7,060)	(7,060)
	$(30,125)	$(30,125)

14. Income Taxes

For certain gas transportation and marketing and petrochemical operations, charges to customers are based on cost-of-service agreements. Since income taxes related to these operations are a component of the charges, the billing for such income taxes on either a taxes payable or tax allocation basis does not affect net income.

Income tax expense varies from the amounts that would be computed by applying the Canadian federal and provincial income tax rates to income before income taxes, interest of others in income of subsidiaries and extraordinary items as shown in the following table:

Year Ended December 31	1987	1986	1985
			(Thousands of dollars)
Income before income taxes, interest of others in income of subsidiaries and extraordinary items	$269,203	$232,768	$355,514
Add (deduct)			
Cost of service activities			
Gas Transportation & Marketing	(185,884)	(199,267)	(203,304)
Petrochemicals	(70,826)	(70,460)	(66,240)
Equity component in allowance for funds used during construction	(1,046)	(1,859)	(1,587)
Equity in (earnings) losses of affiliated companies	(12,789)	15,204	7,235
Loss on investments	18,146	30,125	—
	$ 16,804	$ 6,511	$ 91,618
Effective Canadian tax rate	50.6%	48.8%	47.9%
Calculated income tax expense	$ 8,503	$ 3,177	$ 43,885
Add (deduct) adjustments to income taxes resulting from—			
Royalties, lease rentals and mineral taxes payable to the Crown	3,685	11,848	35,797
Petroleum and gas revenue tax	—	(12,250)	24,388
Resource allowance on Canadian production income	(4,174)	(17,482)	(50,671)
Earned depletion	—	(4,831)	(9,507)
Provincial income tax abatement	—	2,338	4,578
Alberta royalty tax credit	(3,174)	(4,771)	(4,000)
Non-allowable depreciation and depletion	1,265	11,627	13,566
Earnings from foreign subsidiaries with lower effective tax rates	(5,827)	(2,737)	(5,047)
Utilization of losses for tax purposes	(35,659)	(34,762)	—
Other	(64)	(5,175)	(2,200)
	(35,445)	(53,018)	50,789
Add income taxes billed under cost-of-service contracts	109,786	114,632	105,103
Income tax expense	$ 74,341	$ 61,614	$155,892
Current income taxes	$ 6,994	$ 26,982	$ 75,340
Deferred income taxes	67,347	34,632	80,552
	$ 74,341	$ 61,614	$155,892

Deferred income taxes in each of the three years arose from differences of a timing nature between income for accounting purposes and taxable income in the jurisdictions in which the Corporation and its subsidiaries operate. The principal timing difference relates to the deductions for tax purposes, in respect to plant, property and equipment, in excess of amounts currently charged to operations.

In some cost-of-service operations the Corporation recovers in current revenues only taxes payable and not deferred taxes. Accordingly, the above provision for income taxes excludes deferred income taxes of $12,502,000 in 1987, $12,957,000 in 1986 and $16,400,000 in 1985 and an accumulated amount of $249,317,000 at December 31, 1987. These deferred income taxes relate principally to the deduction for tax purposes, in respect of plant, property and equipment, in excess of amounts charged to operations.

15. Extraordinary Items

(a) For the Year Ended December 31, 1986

	(Thousands of dollars)
Provision for write-down to estimated net realizable value of the portion of the investment in Husky Oil Ltd. held for sale (net of income taxes of $6,900)	$ (7,800)

In December 1986, the Corporation's Board of Directors approved an agreement whereby 57% of the investment in Husky was held for sale with the remainder being held as a long term investment. For accounting purposes, effective December 1, 1986, the accounts of Husky ceased to be consolidated and the remaining long term interest of approximately 24.4%, being approximately 43% of the previous investment in Husky, was accounted for by the equity method. The portion of the Corporation's investment in Husky held for sale was written down to estimated net realizable value, and after providing for all estimated expenses relating to this transaction, an extraordinary loss of $7,800,000 was recorded.

(b) For the Year Ended December 31, 1985

	(Thousands of dollars)
Provision for the write-down of the linear low-density polyethylene plant (net of income taxes of $144,658)	$(157,342)
Loss on dilution of ownership in Husky Oil Ltd.	(58,921)
Provision for write-down of an engineering division to estimated realizable value (net of income taxes of $6,099)	(10,523)
Gain on disposition of polyvinyl chloride plant (net of income taxes of $2,304)	10,264
	$(216,522)

The Corporation reduced the carrying value of its investment in its linear low-density polyethylene plant to approximately $125,000,000, because at the time it was not certain that the investment would be recovered from future cash flow.

The Corporation recorded a loss relating to the dilution of its ownership in Husky due to the conversion by other shareholders of Husky's convertible preferred shares into common shares.

16. Changes in Non-Cash Working Capital

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
Funds on deposit	$ 138,050	$(138,050)	$ —
Secured bond	—	157,500	(157,500)
Receivables	(105,021)	378,554	(18,744)
Inventories	(6,913)	114,976	(1,320)
Assets held for sale	358,998	(358,998)	111,142
Prepaid expenses	(1,073)	409	975
Bank loans	(4,823)	5,839	(19,269)
16-1/4% Unsecured debentures	(138,050)	138,050	—
Bank indebtedness	—	(154,625)	154,625
Accounts payable and accrued liabilities	30,518	(342,440)	(3,173)
Income taxes payable	(1,978)	(68,527)	(5,999)
Dividends payable	(5,373)	772	2,488
Changes in non-cash working capital	264,335	(266,540)	63,225
Reclassification and other items not having a cash effect			
Estimated cash proceeds on disposition of the Husky investment less the net working capital effect from deconsolidation in 1986	(358,998)	294,540	—
Other items	15,109	(30,679)	(24,681)
Changes in non-cash working capital having a cash effect	$ (79,554)	$ (2,679)	$ 38,544

These changes relate to the following activities:

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
Operating activities	$ (82,102)	$ (19,345)	$ 59,627
Investment activities	7,921	15,894	(23,571)
Financing activities	(5,373)	772	2,488
	$ (79,554)	$ (2,679)	$ 38,544

17. Pension Plans

The Corporation has pension plans covering substantially all employees. Pensions at retirement are related to years of service and remuneration during the last years of employment. Actuarial reports are prepared annually by independent actuaries for accounting and funding purposes. Assumed future rates of return on assets of the plans averaged 7%. Estimated projected benefit obligations of the plans were determined using discount rates averaging 7% and long term salary and wage escalation rates averaging 6%.

Net pension expense for 1987 consisted of the following:

	(Thousands of dollars)
Current service costs	$ 11,159
Interest cost on projected benefit obligations	8,224
Estimated return on assets	(9,906)
Net total of other components	(521)
	8,956
Less amounts recoverable under cost-of-service contracts	(4,801)
Net pension expense	$ 4,155

The status of the pension plans at December 31, 1987, is as follows:

	(Thousands of dollars)
Estimated obligations	
Projected benefits based on service to date and present remuneration	$ 78,006
Additional amounts related to projected salary and wage increases	58,835
Total projected benefit obligations	136,841
Assets available at adjusted market value	158,370
Excess of assets over projected benefit obligations	$ 21,529
Amount recognized in the consolidated balance sheet	
Accrued pension obligation	$ 4,512

18. Contingencies and Commitments

(a) The Corporation has a lease agreement in connection with its head office building. At December 31, 1987, the future minimum rental payment provided in the agreement, which expires in 1997, is approximately $16,099,000 for 1988 and 1989 and $17,749,000 for 1990 to 1992. Rental expense in 1987 was $16,099,000.

The agreement provides that, on or after January 1, 1995, the Corporation offers to purchase the property at the expiration of the lease for $157,500,000.

The annual cost of other leases is not material.

(b) Various lawsuits and claims are pending by and against the Corporation. It is the opinion of management that final determination of these claims will not materially affect the financial position or operating results of the Corporation.

19. Segmented Information

(a) Financial Information by Business Segment

The management of the Corporation has determined that the following are the principal business segments of the Corporation:

Gas Transportation & Marketing	– transportation and marketing of natural gas.
Petrochemicals	– production, transportation and marketing activities for various petrochemical products.
Petroleum	– exploration, development, production, refining and marketing activities for crude oil and natural gas, together with consulting and research.
Manufacturing	– design, development, manufacture and marketing of various products primarily for use in the resource, transportation and telecommunications industries.

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
Revenue			
Gas Transportation & Marketing	$1,167,650	$1,245,429	$1,529,957
Petrochemicals	1,021,406	724,790	756,819
Petroleum	49,900	626,153	978,886
Manufacturing	103,482	105,911	97,404
	2,342,438	2,702,283	3,363,066
Less intersegment revenue			
Gas Transportation & Marketing	11,627	10,102	2,172
Petroleum	8,373	11,215	13,658
	20,000	21,317	15,830
	$2,322,438	$2,680,966	$3,347,236
Operating income (loss)			
Gas Transportation & Marketing	$ 320,221	$ 338,670	$ 345,478
Petrochemicals	202,886	73,640	48,036
Petroleum	(2,284)	158,179	266,531
Manufacturing	7,375	2,732	13,527
	528,198	573,221	673,572
Interest expense	(242,729)	(284,292)	(315,915)
Allowance for funds used during construction	2,501	3,480	3,171
Equity in earnings (losses) of affiliates	12,789	(15,204)	(7,235)
Loss on investments	(18,146)	(30,125)	–
Miscellaneous income and other (deductions)	(13,410)	(14,312)	1,921
Income taxes	(74,341)	(61,614)	(155,892)
Interest of others in income of subsidiaries	(15,732)	(63,157)	(65,511)
Income before extraordinary items	179,130	107,997	134,111
Extraordinary items	–	(7,800)	(216,522)
Net income (loss)	$ 179,130	$ 100,197	$ (82,411)
Identifiable assets			
Gas Transportation & Marketing	$2,231,529	$2,224,273	$2,308,412
Petrochemicals	1,195,117	1,083,575	1,108,049
Petroleum	758,173	895,144	2,270,621
Manufacturing	240,047	275,641	265,863
Other	260,882	284,319	265,409
	$4,685,748	$4,762,952	$6,218,354

Year Ended December 31	1987	1986	1985
			(Thousands of dollars)
Plant, property and equipment additions			
Gas Transportation & Marketing	$ 85,288	$ 79,506	$ 79,201
Petrochemicals	84,690	61,429	11,313
Petroleum	16,286*	182,390*	295,424*
Manufacturing and Other	13,532	3,050	1,380
	$ 199,796	$ 326,375	$ 387,318
Depreciation and depletion			
Gas Transportation & Marketing	$ 96,573	$ 97,258	$ 91,620
Petrochemicals	61,967	59,559	74,949
Petroleum	13,855	130,480	138,267
Manufacturing	5,676	5,247	5,344
	$ 178,071	$ 292,544	$ 310,180

* *Net of Petroleum Incentive Program grants of $1,489 in 1987, $84,591 in 1986 and $123,953 in 1985.*

(b) Financial Information by Geographic Area

Year Ended December 31	1987	1986	1985
			(Thousands of dollars)
Revenue			
Canada	$2,124,427	$2,532,691	$3,197,026
United States	119,081	83,241	87,955
Other	78,930	65,034	62,255
	$2,322,438	$2,680,966	$3,347,236
Operating income (loss)			
Canada	$ 510,899	$ 572,744	$ 658,562
United States	13,628	827	6,795
Other	3,671	(350)	8,215
	528,198	573,221	673,572
Interest expense	(242,729)	(284,292)	(315,915)
Allowance for funds used during construction	2,501	3,480	3,171
Equity in earnings (losses) of affiliates	12,789	(15,204)	(7,235)
Loss on investments	(18,146)	(30,125)	—
Miscellaneous income and other (deductions)	(13,410)	(14,312)	1,921
Income taxes	(74,341)	(61,614)	(155,892)
Interest of others in income of subsidiaries	(15,732)	(63,157)	(65,511)
Income before extraordinary items	179,130	107,997	134,111
Extraordinary items	—	(7,800)	(216,522)
Net income (loss)	$ 179,130	$ 100,197	$ (82,411)
Identifiable assets			
Canada	$4,441,402	$4,556,257	$5,961,224
United States	131,210	86,097	127,479
Other	113,136	120,598	129,651
	$4,685,748	$4,762,952	$6,218,354

(c) Principal Customers

The following information discloses the revenue generated by customers who individually account for more than 10% of the Corporation's consolidated revenue:

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
Northwest Alaskan Pipeline Company (i)	$ 455,974	$ 567,253	$ 834,083
TransCanada PipeLines Limited (ii)	$ 290,592	$ 322,074	$ 324,788
Dow Chemical Canada Inc. (iii)	$ 307,636	$ 313,846	$ 295,082

(i) Most of the sales of natural gas to the United States are to Northwest Alaskan Pipeline Company, which in turn sells the gas to other U.S. pipeline companies.

(ii) TransCanada PipeLines Limited is one of the major shippers of natural gas through the pipeline systems of the Alberta Gas Transmission Division and TQM Pipeline.

(iii) Dow Chemical Canada Inc. is under a long term purchase contract for ethylene production.

(d) Export sales

Export sales from the Corporation's Canadian operations amounted to the following:

(Thousands of dollars)

Year Ended December 31	1987	1986	1985
United States	$ 838,869	$ 751,954	$1,032,518
Other	88,899	7,831	15,248
	$ 927,768	$ 759,785	$1,047,766

20. Subsequent Event

On February 22, 1988, the Corporation acquired 13,004,175 common shares of Polysar Energy & Chemical Corporation ("Polysar"), formerly Canada Development Corporation, for a total purchase price of $208,067,000. At December 31, 1987, the Corporation owned 6,000,000 common shares of Polysar or approximately 9.7% of Polysar's issued and outstanding common shares (see Note 5). The Corporation now owns 19,004,175 common shares of Polysar or approximately 31% of the issued and outstanding common shares and approximately 25% of the outstanding voting securities.

Summarized Quarterly Financial Data

(Thousands of dollars except for share data)

Three months ended	March 31 1987	March 31 1986	June 30 1987	June 30 1986	September 30 1987	September 30 1986	December 31 1987	December 31 1986
Revenue	**$541,980**	788,921	**528,357**	639,399	**585,323**	641,027	**666,778**	611,619
Operating income	**$110,030**	131,128	**133,403**	165,068	**127,671**	152,190	**157,094**	124,835
Income before extraordinary items	**$ 33,557**	26,257	**45,030**	37,033	**47,016**	35,472	**53,527**	9,235
Extraordinary items	**$ —**	—	**—**	—	**—**	—	**—**	(7,800)
Net income (loss)	**$ 33,557**	26,257	**45,030**	37,033	**47,016**	35,472	**53,527**	1,435
Net income (loss) per common share before extraordinary items								
Basic	**$ 0.09**	0.04	**0.19**	0.12	**0.20**	0.11	**0.22**	(0.09)
Fully diluted	**$ 0.08**	0.04	**0.19**	0.12	**0.20**	0.10	**0.20**	(0.09)
Net income (loss) per common share after extraordinary items								
Basic	**$ 0.09**	0.04	**0.19**	0.12	**0.20**	0.11	**0.22**	(0.15)
Fully diluted	**$ 0.08**	0.04	**0.19**	0.12	**0.20**	0.10	**0.20**	(0.14)
Market price per common share								
High	**$ 9¼**	7¼	**9½**	5¾	**11½**	5⅜	**11½**	6½
Low	**$ 5⅝**	5⅝	**7¾**	4.60	**9**	4.35	**7**	5⅛

Oil and Gas Activities

Reserves

The following information provides estimated quantities of the Corporation's proved oil and gas reserves, which are all in Canada.

	Oil	Gas
Proved developed and undeveloped reserves*		
At January 1, 1986*	4,098	284,346
Revisions of previous estimate*	(1,439)	(92,588)
Extensions, discoveries and other additions	760	17,400
Production	(160)	(8,600)
At December 31, 1986	3,259	200,558
Revisions of previous estimate	**62**	**15,186**
Extensions, discoveries and other additions	**79**	**12,994**
Production	**(242)**	**(11,062)**
At December 31, 1987	**3,158**	**217,676**
Proved developed reserves		
At December 31, 1985*	2,332	153,281
At December 31, 1986*	2,543	149,153
At December 31, 1987	**2,414**	**152,387**

**Restated*

	Oil	Gas
Corporation's proportionate interest in proved reserves of Companies accounted for by the equity method*		
At December 31, 1985**	49,212	125,643
At December 31, 1986**	37,890	115,671
At December 31, 1987	**36,252**	**137,228**

** Represents the Corporation's proportionate interest in proved developed oil and gas reserves of Husky.*
*** For comparative purposes the Corporation's indirect proportionate interest in Husky of 42.5% at December 31, 1987 has been used (Note 5 of the Notes to Consolidated Financial Statements).*

Crude oil, including natural gas liquids, is expressed in thousands of barrels. A barrel represents a stock tank barrel equivalent to 42 U.S. gallons or 35 Imperial gallons. Natural gas is expressed in millions of cubic feet measured at 60° F and 14.65 psia.

Volumes represent the net reserves owned after deduction of royalties, reversionary interests, and net profit interests owned by others.

Landholdings

The landholding acreage of the Corporation and of Husky, which is accounted for by the equity method, is summarized below in thousands of acres:

	Corporation		Husky (2)	
	Gross (3)	Net (4)	Gross (3)	Net (4)
Canada				
Western Canada				
Alberta	1,084	538	2,526	1,554
Saskatchewan	15	9	855	806
British Columbia	4	1	193	69
Total Western Canada	1,103	548	3,574	2,429
Frontier Areas (5)				
Nova Scotia (offshore)	—	—	295	114
Newfoundland (offshore)	—	—	990	166
Northwest Territories	—	—	124	2
Beaufort Sea	—	—	494	39
Total Frontier Areas	—	—	1,903	321
Total Canada	1,103	548	5,477	2,750
Total International	—	—	6,897	1,890

(1) Landholding interests in gross acreage are subject to royalties and other non-working interests. Net acreage is based on the percentage interest owned in gross acreage without allowance for production payments or special limitations which may restrict the working interests.
(2) Includes 100% of Husky's landholdings. Not included are 374,554 gross acres in Alberta, Saskatchewan and British Columbia in which Husky owns overriding royalty interests.
(3) A gross acre is an acre in which a working interest is owned. The number of gross acres is the total number of acres in which an interest is owned.
(4) The number of net acres is the sum of the fractional working interests owned in the gross acres expressed in whole numbers.
(5) Exploration Agreements, which have been negotiated with the Government of Canada, began for the Atlantic offshore, Beaufort Sea and the Northwest Territories in 1984. The terms of each agreement establish a work program which includes the drilling of at least one well and the obligation to relinquish 50% of the lands during the initial term.

		1987	1986	1985	1984
Operating Results					
Revenue	$	2,322,438	2,680,966	3,347,236	3,793,533
Operating income	$	528,198	573,221	673,572	676,988
Income before extraordinary items	$	179,130	107,997	134,111	155,268
Net income (loss)	$	179,130	100,197	(82,411)	203,350
Net income (loss) to common shareholders	$	129,834	16,126	(167,922)	125,358
Assets					
Working capital	$	79,825	324,766	32,978	43,341
Plant, property and equipment (net)	$	3,228,483	3,217,531	4,863,581	5,190,296
Total assets	$	4,685,748	4,762,952	6,218,354	6,342,683
Capitalization					
Long term debt—cost-of-service	$	1,787,958	1,763,158	1,725,949	1,769,676
—non-cost-of-service	$	647,273	697,725	978,285	1,130,870
Preferred shares—cost-of-service	$	125,197	194,213	205,096	212,286
—non-cost-of-service	$	203,711	632,695	656,861	568,308
Common equity (1)	$	1,302,797	648,707	563,270	742,923
Total capitalization	$	4,066,936	3,936,498	4,129,461	4,424,063
Cash Flow Data					
From operations	$	395,641	527,942	669,393	503,145
Spending on plant, property and equipment	$	199,796	326,375	387,318	624,073
Capital raised—long term debt	$	218,235	100,189	123,788	411,197
—preferred equity	$	—	—	96,844	—
—common shares and warrants	$	31,184	97,889	27,540	23,787
Dividends—preferred shareholders	$	49,296	84,071	86,636	77,992
—common shareholders	$	77,009	54,451	51,619	49,447
Common Share Statistics					
Net income (loss) per share					
Basic	$	0.70	0.12	(1.31)	1.02
Fully diluted	$	0.67	0.12	(1.31)	0.77
Dividends paid per share	$	0.40	0.40	0.40	0.40
Outstanding—year end (thousands)		211,484	141,841	130,658	125,254
—average (thousands)		185,321	134,655	128,087	123,203
Common equity per share at year end	$	5.76 (2)	4.22 (2)	4.31	5.93
Market prices—high-low	$	11-1/2 - 5-5/8	7-1/4 - 4.35	7-5/8 - 5-1/2	8-1/8 - 6-3/8
—year end	$	10.00	5-7/8	7-1/8	7-1/8
Ratios					
Common shareholder					
Return on average common equity	%	13.3	2.7	*	18.1
Dividend payout	%	59.3	*	*	39.4
Dividend yield (year-end market price)	%	4.0	6.8	5.6	5.6
Capital					
Long term debt to common equity		1.9:1	3.8:1	4.8:1	3.9:1
Interest coverage		2.0x	1.7x	2.0x	1.9x

** Not comparable*

(1) Includes convertible debentures and warrants.

(2) Calculation includes the effect from conversion of the convertible debentures and warrants.

(Thousands of dollars except for share data)

1983	1982	1981	1980	1979	1978	1977
3,823,005	3,500,066	2,666,120	2,114,520	1,218,541	431,952	348,779
544,063	511,699	387,694	363,455	253,252	120,101	125,639
150,733	150,524	127,441	141,775	115,283	85,906	57,471
35,128	150,524	127,441	141,775	115,283	85,906	57,471
(44,435)	91,953	94,607	106,485	87,168	65,841	44,929
63,923	16,168	11,889	60,457	121,512	125,431	64,305
5,541,801	4,870,523	3,753,956	2,549,880	2,114,209	1,137,686	923,420
6,760,610	6,333,029	5,012,175	3,671,523	3,144,422	2,062,096	1,443,625
1,712,449	1,469,193	1,004,786	697,046	627,297	678,929	648,018
1,737,038	1,344,150	1,279,842	412,450	470,421	172,343	119,670
221,093	228,627	174,771	184,647	193,658	203,593	210,597
579,814	597,495	266,464	308,076	169,923	189,000	—
639,413	692,479	627,846	527,295	402,061	318,245	270,546
4,889,807	4,331,944	3,353,709	2,129,514	1,863,360	1,562,110	1,248,831
505,380	495,194	307,133	432,074	206,959	89,552	109,781
933,807	1,221,953	1,371,230	569,389	313,905	233,154	233,988
730,304	1,088,244	1,255,835	220,130	152,262	197,594	409,935
—	402,539	—	192,275	—	182,028	72,552
16,741	5,105	4,881	1,761	2,164	211	458
79,563	64,701	32,834	36,898	28,115	21,543	13,244
47,581	46,003	42,837	37,508	28,840	22,780	20,247
(0.38)	0.80	0.88	1.08	0.98	0.77	0.55
(0.38)	0.74	0.80	0.90	0.81	0.71	0.53
0.40	0.40	0.38666	0.36	0.30833	0.25907	0.2448
120,664	116,189	110,961	103,351	92,253	87,354	83,474
118,478	114,341	107,583	99,001	89,223	85,083	82,263
5.30	5.96	5.66	5.10	4.36	3.64	3.24
9-1/2-6.00	9-7/8-5-1/8	14-3/8-7-1/4	13-3/8-8.00	9-3/8-4-7/8	5-1/2-4-5/8	5-1/2-4-1/4
7-1/4	8-7/8	9-1/2	13.00	8-5/8	5.00	5-3/8
*	13.9	16.4	22.9	24.2	22.4	17.6
*	50.0	45.3	35.2	33.1	34.6	45.1
5.5	4.5	4.1	2.8	3.6	5.2	4.6
5.4:1	4.1:1	3.6:1	2.1:1	2.7:1	2.7:1	2.8:1
1.7x	1.6x	1.8x	3.4x	3.4x	2.8x	4.0x

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Foothills Pipe Lines (Yukon) Ltd. (50%)
Trans Québec & Maritimes Pipeline Inc. (50%)
Pan-Alberta Gas Ltd. (50.005%)

Petroleum
Husky Oil Ltd. (42.5%)
Novalta Resources Ltd. (100%)

Petrochemicals
Novacor Chemicals Ltd. (100%)
The Alberta Gas Ethylene Company Ltd. (100%)
Alberta Gas Chemicals Ltd. (50%)

Manufacturing
Grove Italia S.p.A. (100%)
NovAtel Communications Ltd. (50%)

Consulting & Research
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